

OVERSIGHT OF THE DISASTER ASSISTANCE PROGRAMS

Y 4. AG 8/3: S. HRG. 103-669

Oversight of the Disaster Assistance...

HEARING BEFORE THE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY UNITED STATES SENATE ONE HUNDRED THIRD CONGRESS SECOND SESSION ON OVERSIGHT OF THE DISASTER ASSISTANCE PROGRAMS

APRIL 13, 1994

Printed for the use of the
Committee on Agriculture, Nutrition, and Forestry



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OVERSIGHT OF THE DISASTER ASSISTANCE PROGRAMS

WEDNESDAY, APRIL 13, 1994

U.S. SENATE,
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
WASHINGTON, DC.

The committee met, pursuant to notice, at 10:22 a.m., in room SR-332, Russell Senate Office Building, Hon. Patrick J. Leahy, Chairman of the committee, presiding.

Present or submitting a statement: Senators Leahy, Lugar, Conrad, and Coverdell.

STATEMENT OF HON. PATRICK G. LEAHY, U.S. SENATOR FROM VERMONT

The CHAIRMAN. Because of the votes on the floor and conflicting schedules, I know a number of Senators are between two different places, but will be here at one time or another during this hearing.

One of the major areas of oversight of this committee is in Agriculture disaster programs. They are very important to farmers. Seeing Senator Conrad here, I recollect in 1988 when a number of the Members of this committee went to Montana, North Dakota, and South Dakota, because of the very serious drought. We looked at the problems and talked with farm families. We came back and reported to the rest of the Senate and in less than a month passed the most generous disaster bill, I believe, the Senate ever had.

I do not think there is anybody in America who really felt that it was anything but a justified disaster bill. We are a generous Nation and we try to help our people when they are suffering. We have all seen the tragic photographs of the farms destroyed by floods in the Midwest. Our hearts, but also our Federal dollars have gone out to those farmers.

Yet, when we do oversight we find there is another side to disaster programs. It would appear that sometimes these disaster programs have been misused and that is too mild a word. They have been raided and they have been robbed in a way that was never intended by the American taxpayers and the Congress. What it does, of course, is put an onus on all farm programs and it puts in jeopardy those programs that are needed to continue the production of food and fiber in our country.

In fact, we will see that sometimes it takes money out of the pockets of those farmers who really need it and puts it into the pockets of people who are nothing more than common thieves. So the hearing this morning is going to be a little different from many

Congressional hearings. Normally we have the Secretary of Agriculture or the Inspector General testify.

At one time I was the prosecutor and I enjoyed that work very much. I also, as a prosecutor realized you have the heads of offices, but then you have very often those who actually do the work—the auditors and the investigators who do the work in the field. When I was a prosecutor, I knew that they were the people that had to bring me the evidence necessary for convictions.

So I thought this morning instead of hearing from high officials and the inspector general, we would have as a principal witness, Mr. Charlie Womble who is a field auditor from the inspector general's Atlanta office. I am going to go through a number of questions here.

Incidentally, just to put it into order, for those of you who are not familiar with agricultural programs, special disaster programs have been enacted every year since 1986. This year the administration has proposed comprehensive crop insurance disaster reform legislation. We are going to have the present Head of the Agricultural Stabilization and Conservation Service, Grant Buntrock, and the Manager, of the Federal Crop Insurance Corporation, Ken Ackerman, here this morning. I should note that Mr. Ackerman was until recently one of the senior staff members of this committee and was very well respected by all of us.

Then, we will have a full hearing on the administration's reform proposal at a later date. Senator Conrad, did you have an opening statement?

Senator CONRAD. No, Mr. Chairman, I think with the witness panel that we have, I would not want to delay our turning to them.

The CHAIRMAN. Thank you.

STATEMENT OF CHARLIE WOMBLE, SUPERVISORY AUDITOR, OFFICE OF INSPECTOR GENERAL, U.S. DEPARTMENT OF AGRICULTURE, ATLANTA, GEORGIA; ACCOMPANIED BY KEN ACKERMAN, MANAGER, FEDERAL CROP INSURANCE CORPORATION, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC.; GRANT BUNTROCK, ADMINISTRATOR, AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC.; JAMES R. EBBITT, ASSISTANT INSPECTOR GENERAL FOR AUDIT, OFFICE OF INSPECTOR GENERAL, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC.; AND WILLIAM E. GAHR, ASSOCIATE DIRECTOR, FOOD AND AGRICULTURAL ISSUES, GAO, WASHINGTON, DC.

Mr. Womble, let us start with you. Working out of the Atlanta office, you did audit disaster payments in Mitchell County, Georgia; is that correct?

Mr. WOMBLE. Yes, sir, Mr. Chairman, that is correct.

The CHAIRMAN. How did you pick Mitchell County?

Mr. WOMBLE. We received an anonymous hot line complaint alleging that certain producers in Mitchell County were fraudulently receiving ASCS disaster payments.

The CHAIRMAN. In fact the IG's office often gets tips of things to look at on this hot line; do they not?

Mr. WOMBLE. Yes, sir, that is correct.

The CHAIRMAN. How many producers did you audit and how did you pick the producers to audit?

Mr. WOMBLE. We analyzed the farming operations of 48 producers who were farming on 26 farms. They were selected either because they had been identified in the hot line complaint or they had received disaster payments in excess of \$50,000.

The CHAIRMAN. These disaster payments, what type of crops were they for?

Mr. WOMBLE. The crops that we looked at were primarily squash and cucumbers.

The CHAIRMAN. Why did you pick those particular crops? There are a lot of crops being raised in Georgia. Why those particular ones?

Mr. WOMBLE. Squash was actually mentioned in the hot line complaint itself and squash and cucumbers represented the crops having the highest dollars for disaster payments in Mitchell County.

The CHAIRMAN. If somebody raises squash in Georgia, is that usually the only crop they raise or do they raise other crops in that same land?

Mr. WOMBLE. Most normally, the farmers in Georgia would raise other crops in addition to the squash crops that they might be growing.

The CHAIRMAN. What is the normal sequence, normal season sequence, during a year, in raising crops?

Mr. WOMBLE. For those farms that we looked at in Mitchell County, in Georgia most of them involved double-cropping which means that the squash crop was planted immediately after another crop. We found that oftentimes the squash followed either cotton or peanuts.

The CHAIRMAN. Using the same field, same land?

Mr. WOMBLE. Yes, sir, the same field and same land.

The CHAIRMAN. Was there a deadline for planting fall squash in Mitchell County, Georgia?

Mr. WOMBLE. Yes, sir. The deadline was established at September 20.

The CHAIRMAN. Why does there have to be a deadline? Why do they establish one?

Mr. WOMBLE. They established the deadline to ensure that there would be sufficient time after planting for the crop to mature before frost.

The CHAIRMAN. So you had a date that they had to plant by. Now if they had to plant by that date, that meant that the other crops, whether it is cotton or peanuts, had to be out of the fields, did they not?

Mr. WOMBLE. Yes, sir, Mr. Chairman, that is correct.

The CHAIRMAN. Did you find any instances where they said that they were planting squash, but indeed either cotton or peanuts were still in the field at the time they were supposedly planting squash?

Mr. WOMBLE. Yes, sir. We identified 12 farms where the cotton or peanuts had not been harvested by the time the squash were reported to have been planted. When we went to the cotton gin, we were able to identify the date the cotton was harvested and based

on that information, we concluded that, in fact, the cotton was still in the field by the established planting date.

The CHAIRMAN. Had there been a disaster payment request for this squash that was supposedly planted where you discovered other things were planted?

Mr. WOMBLE. That is correct, yes, sir.

The CHAIRMAN. So did you determine that something else was in those fields, but not squash?

Mr. WOMBLE. Yes, sir, we did. We determined that, in fact, the cotton and/or peanuts in these instances were still in the field at the time the squash were reported to have been planted and at the time of the deadline.

The CHAIRMAN. So a request was being made for disaster payment for a crop that was never there?

Mr. WOMBLE. That is correct.

The CHAIRMAN. The 48 producers, your data shows, if I understand, that half of them, 24 submitted questionable invoices. Did these farmers have to produce evidence that they actually had done the things necessary for planting—buy fertilizer, seed, do whatever has to be done?

Mr. WOMBLE. The county committee determined that as long as a producer could show evidence of production, then it was not necessary to provide evidence that the crop, in fact, the seed, etc., had been purchased.

The CHAIRMAN. Then how do you show the production? Do you do it by invoices?

Mr. WOMBLE. Yes, sir, they brought in evidence of their production and where they sold it. They would bring in an invoice showing that, in fact, they had sold squash.

The CHAIRMAN. So did they bring in those invoices?

Mr. WOMBLE. Yes, sir, they brought them in, but in 10 of the 18 cases where we identified that there had been improper or incorrect information, those producers only brought in one invoice to support one sale on that farm. This seemed unusual.

The CHAIRMAN. Why is that unusual?

Mr. WOMBLE. Normally in the squash business, the producer harvests his squash over a period of time involving several days and there would actually be multiple harvests. So you would expect that the producer would have multiple sales and deliveries to the produce buyers. In these 10 cases, they brought in evidence showing they only had that one sale.

The CHAIRMAN. Did you go to the buyers to see whether they could verify this?

Mr. WOMBLE. Yes, sir, we did.

The CHAIRMAN. What did you find?

Mr. WOMBLE. One of the buyers that we visited told us that, in fact, he had bought the squash.

The CHAIRMAN. Did he have records?

Mr. WOMBLE. No, sir, he did not have any records. He told us that his records had been damaged and he had thrown them away. So he did not have any records to prove it.

The CHAIRMAN. Canceled checks or anything like that?

Mr. WOMBLE. No, sir, he said that all of the purchases were made in cash. So he had no canceled checks to support the purchases.

The CHAIRMAN. Well I do not want to interject any levity in here. I recall this skit that used to be done on Saturday Night Live by a person called church lady who used to say, how convenient. With these producers and buyers, was this an arm's length transaction or was there an established relationship between these people?

Mr. WOMBLE. They all lived in the same general vicinity. Beyond that, we did not establish a relationship.

The CHAIRMAN. What about the producers, say the 30 or so producers, any relation between them?

Mr. WOMBLE. We identified that of the 31 that we concluded had provided inaccurate information, 15 were members of one family and three others were closely associated with that family. They either worked with the family, or otherwise associated with the family.

The CHAIRMAN. Just to put this into context, these 18 producers, in 1990 and 1991, how much money are we talking about? How much in disaster payments did they receive?

Mr. WOMBLE. In those 2 years, these 18 people received \$862,109 in disaster payments.

The CHAIRMAN. \$862,109?

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. So we are not talking "penny annie" here?

Mr. WOMBLE. No, sir, we are not.

The CHAIRMAN. When you went county-wide in this one county, Mitchell County, how much of the disaster assistance program funds were spent based on what you feel is inaccurate information, county-wide?

Mr. WOMBLE. Of those that we looked at, we concluded that in excess of \$1.3 million was received spent improperly, based on inaccurate information.

The CHAIRMAN. In that county?

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. I do not mean to put words in your mouth, but what it appears is what you found is that either the crops were not planted at all or if there was any planting being done, it was being planted for disaster payments not for the normal production of crops?

Mr. WOMBLE. Yes, sir, that is correct.

The CHAIRMAN. Mr. Ackerman, is crop insurance available for squash at this time?

Mr. ACKERMAN. No, it is not.

The CHAIRMAN. We are talking about broad crop insurance reform legislation. I think it is something we all agree is needed. You are going to have more producers receiving crop insurance. How do you make sure something like this does not happen?

Mr. ACKERMAN. Mr. Chairman, we do two principle things. Of the 50 odd crops that crop insurance does cover, we would replace the disaster programs in total with an extended crop insurance program. The crop insurance program has a number of internal controls which we acknowledge are not perfect; but these internal controls would in many cases have picked up these problems.

For a crop like squash which we do not cover, we would create a standing disaster program and we would incorporate into that some of the internal controls from crop insurance. For instance, we would require actual yield histories for establishing yields under the disaster program. We would require acreage reports being made up front by producers, rather than allowing them to report, as in the case of the inspector general report, reporting say 50 acres at the beginning of the season and then 200 when they applied for disaster aid.

On this question of invoices, we have the same rule, that the same problem with multiple invoices would have been picked up by our compliance system. We have compliance cases right now on this very type of problem involving other crops. So we would be tightening it from those two directions.

The CHAIRMAN. Would that have helped, Mr. Womble?

Mr. WOMBLE. Yes, Sir, I believe that these controls would reduce the opportunity for such abuses to occur.

The CHAIRMAN. Mr. Buntrock, what kind of steps is the administration taking to address these problems? I know you and I have actually discussed this already and you are certainly well aware of Mr. Womble's report. What is being done?

Mr. BUNTROCK. Mr. Chairman, we certainly are, and of course as you are, we are quite concerned about it. I would just like to go over very briefly some of the steps that we have taken to make certain that we do not have reoccurrences of this and some followup actions that we have taken as a result of it.

Before I begin, I would certainly like to express my appreciation to the Chairman and Members of his committee for the opportunity to be here today to discuss what I consider to be one of the more significant responsibilities that we have in this whole disaster area. As the Chairman well knows and Members of this committee, these disaster programs are very critical and very vital to the farmers in this country and without them over the past few years, I am not so sure that a lot of them would be there today.

It is very unfortunate, of course, that we have a situation that would raise some questions on the credibility of all of these programs as a result of some of these instances. The positive side of it is, I think, it is fair to point out that this is not a widespread situation, as the Chairman has noted at the beginning. It involves some of these crops that direly need something done. It does not lessen the severity of the problem.

I think just to make certain that we have it in context, I believe out of some several billion dollars that we have involved with the administration over the past several years, it involves something in the millions of dollars with these problem crops.

Senator CONRAD. Could you put a finer point on that? If I could, Mr. Chairman, when you talk several million, are we talking about \$5 million, \$10 million or are we talking about \$100, \$200 million?

Mr. BUNTROCK. Senator Conrad, up to this point the various OIG investigations, I think there has been something in the neighborhood of 11 audits that specifically addressed specialty crops. What was found during that course of review was about \$6 million in question on these specialty crops overall.

Now in addition to the things that OIG has found and we have been working very closely with OIG and the GAO to address these problems, we also have put together in cooperation with the Federal Crop Insurance folks a team to go in to several these States that are heavy on the specialty crops. There are five States—Florida, California. We are in North Dakota, in your home State, Senator, to look at some of the crops in that State. The idea being to find more ways that we can tighten this up and address these problems in the interim period and make these programs a lot more responsible.

To give you an idea of some of the specifics the Chairman inquired about, let me just run over some things that we have done, some actions that have been taken. We provided for an electrotonic data inquiry, based on validity checks and cross checks, that are in place at our Kansas City office, where we have the communication with the county offices from the Kansas City office that can highlight some of these potential problems.

We also, of course, have county office reviewers. These are people who are trained in these programs that we have sent out to verify some of these yields in crops and we have concentrated especially on these specialty crops to find out areas that we can take action to tighten these things up.

As a result of this, we have also required from this point on, Mr. Chairman, that for a lot of these specialty crops where we simply do not have the data that we would be comfortable with, we have required that yields, established yields and price data and additional payment approvals, where you come in with a situation like Mr. Womble described, that a lot of these need to come now to the national office for clearance before they can act on these subsequent applications.

We have also provided more flexibility at the local level with local county committees, so that in the event they get a claim with the yield—one of the problems that we have had is on the actual yield, historical yield, baseline and what you might expect some of these crops that we just simply are not that familiar, and do not have the database. We have provided county committees with authority where they know, for example, that some of these crop yields in the area may be based on irrigation, when actually, in some cases it is dryland. We provided authority for these committees to adjust these yields down below what they might have otherwise, taking into consideration the cultural practices.

Another example we have come across is that some of these crops are grown under contract with a seed company and there is a guarantee built in by the company that they would cover a certain amount of production, irrespective of whether it is affected by disaster. We now have provided county offices to deduct that guaranteed production from the company, so that we are not paying on that particular production that is already covered by the company.

These are just a few of the actions that we have taken. What I wanted to add to all of this to support what the Chairman talked about at the beginning. A lot of these actions will certainly improve, and I believe that we have in place now at least have a means of detecting these kind of problems that Mr. Womble talked about before they get out of hand, so we can get after them.

The real fix, if I can put it that way, on these specialty crops is what Mr. Ackerman talked about, and that is this reform package that Secretary Espy has put forth which would give us the authority up front to go out and collect this information in terms of acreage and yields and data and some of the same information that we have on program crops. That would be very very helpful in alleviating a lot of these problems.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you. Senator Lugar?

Senator LUGAR. Thank you very much, Mr. Chairman. I am just curious as to the comment that you just made, Mr. Buntrock. Essentially you pointed out the very important authority that Secretary Espy has called for and I would agree, just having heard your iteration of the criteria you are now attempting to impose that codification of this be essential. Is it conceivable that that authority could proceed even absent the overall fiscal thrust of the proposition that Secretary Espy has?

Specifically, I mean that as I understand the budget conference committee will be commencing as meetings maybe even as early as tomorrow, April 14, and essential at least to the argument that we are entertaining today, any way that we move to a crop insurance program from disaster is the inclusion in this conference of a billion dollars which Secretary Espy has called for. As I understand the Senate has a zero figure in the resolution that came out and the House has \$700 million which makes for a very difficult conference situation to get to a billion, splitting the difference there, it falls somewhat short.

Notwithstanding that, my understanding is also that Secretary Espy has been vigorous in his advocacy of the billion dollar figure in the conference and may have gained some support from conferees. I have no idea where all that stands, but just in background for what we are talking about today, so that all of us understand, as well as the general public, the billion is required, as I understand for the massive reform to occur; namely, what amounts to a substitution of crop insurance in this enhanced form for the normal disaster debates that we have each year in the country.

What if, however, despite the Secretary's advocacy, the budget committee people say, after all we come into this thing with zero in the Senate side, \$700 million in the House side, and hard to get to a conference position of a billion. As a matter of fact, we are just going to punt this one for another year until a farm bill comes along or some other circumstance of that sort. So as a result, you do not have the money.

Under those circumstances, would it still be advisable for this committee or a comparable committee in the House to proceed with these reform changes with regard to data and authority and searching behind the scenes and so forth that you have just suggested? I ask that just as a practical point. What is your view on that?

Mr. BUNTROCK. Mr. Lugar, I would like to respond partially to the question and then have Mr. Ackerman comment further in terms of the aspects of the billion dollars as it refers to the reform package. In terms of some of the things that we currently do in the

administration of these ad hoc programs, and I would like to address it from that standpoint, basically what it boils down to for the nonprogram crops, we really do not have the authority currently to go out and collect data from individual farmers on crops that there is basically no program in effect. In other words, it would be done if we did it on that basis, without this reform package. It would basically be done on a "what if basis" which could be done, I am sure, not without some cost involved in collecting that kind of information.

Also, we would not have anything specific because as we currently operate, we are subject to these ad hoc disaster programs. We do not know, with the uncertainty, not only of the weather but also the uncertainty of the severity and action by the Congress in terms of authorizing these programs. So by having this reform package, of course, you then up front have it in the budget. You budgeted for it. We have a specific charge from the Congress then. In order to administer this program to up front do our homework, prepare ourselves, put this data together and put it in effect for these crops which we otherwise would really not have a basis without some direction from Congress.

Mr. ACKERMAN. Senator Lugar, I will be very brief. I would just make two points. First, as Mr. Buntrock said, one of the biggest problems with record keeping for these ad hoc programs is the fact that they are ad hoc which makes it very difficult to manage them from year to year. That has been one of the biggest problems, for instance, with collecting yield data and keeping it and assessing it, being able to establish historical yields. So if you were to make a couple of legal changes to provide authority, it may not make a big difference because you are still talking about programs that are ad hoc.

Under the legislation that we are proposing, one of the biggest changes is that the disaster program that would exist for the uncovered crops would be a standing program. It would be a permanent program making it possible to manage it year in and year out. On the billion dollars, yes, we believe the billion dollars is essential. That is what we budgeted for this program. That is what we think we need to provide farmers an adequate substitute for disaster bills. Yes, we feel it is essential.

Senator LUGAR. I understand that and that of course will be another argument all by itself because essentially the quid pro quo is that the Congress would be encouraged not to pass a disaster bill and pay for it twice. In other words, there is to be a substitution to go to crop insurance and whether we can all restrain ourselves at that moment, a crisis is still to be determined.

Mr. ACKERMAN. We propose to do more than encourage Congress to show restraint. Our proposal contains an actual amendment to the budget enforcement act creating a specific parliamentary barrier. Crop disaster bills would no longer be considered emergency spending. They would have to be offset by spending cuts.

Senator LUGAR. So you would get a 60-vote to upset the budget situation as opposed to 51?

Mr. ACKERMAN. No, actually as I understand it, you would need basically a parliamentary triple gainer to get around this. On the Senate side, you would have to overcome a point of order with 60

votes. On the House side, you would need action by the House Rules Committee to overcome points of order. Even once you have done all that, it would still be subject to an OMB sequester under the PAYGO rules. So you would have to take a third step of putting in legislative language to side step the PAYGO rules which would first trigger another round of parliamentary objections.

On top of that, you would be acting in a situation where farmers are being provided a specific alternative to disaster aid which they should have received because of a mandatory linkage to commodity programs and Farmers Home Administration loans.

Senator LUGAR. For a variety of reasons, the programs Secretary Espy has has many attractions because you at least fix the liability to the taxpayer every year up front. Then, of course, you also begin to fix many things that were not fixed when we began to get into this disaster business for so many crops. You were here as a valued member of this committee staff at the time, but as I recall, we moved from the program crops which did have the history of planting and yield, all of the regimentation that is required in equating deficiency payments, as the case may be.

As these large disasters came in 1988, it was a good case in point. Nineteen States were covered. People came in from cherry orchards in Michigan, maybe from squash field in Georgia, as the case may be. There were, as I recall, as many as four or 500 different ways in which American farmers make a living, all of them claiming that they ought to have the same privileges as corn farmers and cotton farmers and wheat.

Essentially the Congress acceded to this and sent then to you gentlemen, collectively in your various capacities, the job of paying people who had losses without the crop. So we are really coming now to a fulfillment, I suppose of what was almost bound to occur, whether it be in these counties in Georgia, they were unfortunate enough to be cited this investigation, but this sort of thing probably has occurred through America.

The fact is that we do not have any history and we do not ask up front how much did you plant? As opposed to after the disaster, where no one has any records and makes a claim that he planted four times as much as we think they might have. All sorts of fields are planted or ostensibly have been planted that had never been planted before. This kind of thing is going to continue on without there being changes. The import of my first question is ideally, I understand the Espy program. It provides the money, a crop insurance program for a farmer. You get the insurance; you do not expect to be bailed out by a disaster plan; you then have all of the history requirements, and the data requirements, and the cross compliance. If you have a contract with somebody, or you take an irrigation, all of these things that are very important.

What if there is not the money? That was my problem. Should we continue down the trail with our current disaster program without the data, knowing full well that there are, unhappily, people in America who have done some of the things we have heard today from two counties in Georgia and many counties in America. I do not think we ought to. In other words, it seems to me that there ought to be an interim fix in which we begin to get data on all the other crops in America that are going to come under some plan,

whether it be a disaster plan or crop insurance, with maybe crop insurance being the preferable route.

Mr. ACKERMAN. Senator Lugar, we feel very strongly that this is an area where we agree, a fix is very much needed on these programs. If we are going to go through the process of fixing it, it is worth doing it right the first time. To fix this requires fixing crop insurance, fixing disaster aid, and doing it with the right amount of money. That is why we have been taking the position with the conferees on the budget, that it is very important to go for the full amount of money. Because we do not want to go through this process and end up with a product that still has not solved the problem.

Senator LUGAR. Let me just ask finally, we will know soon how the conferees come out and their product we have presented to the Congress and be adopted, I suppose at some point. So either the program got the money or it did not. Now at that point, can we visit again? In other words, at some point fairly soon we are going to know this objectively, and this is serious enough that we ought not to just have this hearing. Then maybe good things happen with the conferees and maybe they do not. This is a pretty tight budget situation, as you know. A lot of people are heading toward lower figure rather than higher figures. This is a very sell by the Secretary in this position.

We might want to visit again down the trail in 60 days and sort of see where we are, because otherwise you gentlemen are going to have another disaster somewhere in America this year. I hope it will be small, whether it will be ideal. I doubt it. You are not going to have any better data unless you have made some of the fixes, even informally or in an ad hoc fashion than we have this morning. People viewing this hearing are going to say this was a tempest in the teapot. Everybody sort of stirred things around, but we sort of fell back into the same situation.

Mr. BUNTROCK. If I might just comment briefly to follow up with the comments. We certainly have made some fairly substantive kinds of changes here in just recent months to at least put in place a detection system. We also have the group in the field working jointly together and I am convinced that we certainly can minimize, detect immediately the kinds of things that we have talked about, these blatant kinds of things that we have talked about in Georgia. I am convinced that we will have in place something to stop some of these things that have happened in the past.

Now along with that, we still without this reform package, it seems to me that from the standpoint of the producers in what they might have, the problem as you know with any kind of an ad hoc program is simply that there is nothing in the bank, so to speak, there is nothing up front, nothing they can take to the bank with them.

So while this reform package is not going to cover 1,600 nursery crops, it is certainly going to cover the 50 some crops that could be done up front and I would submit that with the additional cost that goes with this package for the time being, in the long run, compared to what we have spent on these disaster programs, even in the event that they are administered very properly and frugally and fairly, you will still save money in the long run by going with

this reform package. Because of this planning that could be done up front, the standpoint of things that we can do administratively that we currently—while we can stop this abuse and this maladministration, and producers getting an unfair advantage that affect other producers, we still will not have the kind of a package under the ad hoc approach that we would have under the reform package. It would be less money.

Senator LUGAR. What is the politics of the situation as you see it, for example, all over America very few farmers have imbibed in the crop insurance situation? That is not true in the Dakotas, for example, and I think Senator Conrad has testified before maybe 50 percent of the farmers there or maybe upwards were in crop insurance, but certainly in my State of Indiana, it would be more like 10 or 20.

Now suddenly, if we pass this bill and if we make a presentation to American agriculture that it is crop insurance or nothing, do farmers in your judgment stand by and say, surely they do not really mean that? In other words, if in fact, we do not all sign up in America, there is going to be a critical mass of difficulty in the event we get in trouble and we come to our Senators and our Members of the House and say, you men and women need to produce, because after all we are constituents and we are in trouble.

You make a point, Mr. Ackerman, you got a triple whip or something in order to keep this parliamentary.

Mr. ACKERMAN. Triple gainer.

Senator LUGAR. Sometimes these disaster programs have been extraordinarily popular. I do not recall a lot of votes against disaster programs. To vote against one is to be perceived so mean spirited as to barely show your face there on the floor. You could do the triple gainer almost by unanimous consent in some cases. So where do you see the psychological equilibrium coming out as to people accepting the fact this is the way that it is?

Mr. ACKERMAN. Senator Lugar, I am very glad you are asking these questions, because we recognize that there is a lot of skepticism in the country and on Capitol Hill about any proposal that will try to prevent ad hoc disaster aid. So I am very glad that you are asking the questions and giving us a chance to respond. Yes, we think the parliamentary barrier is important.

Right now nationwide, the average participation rate in crop insurance is about 33 percent of insurable acres. We have tried to design this program so that every farmer has an opportunity for protection. That is why we have made a point to put in our proposal, and I am looking forward to when we have a hearing to talk about the specifics of it, that we put in it a mandatory linkage, so that every farmer of a program crop or every farmer who gets a loan from the Farmers Home Administration must, as a condition, obtain at least this very inexpensive catastrophic coverage. That will assure that that participation rate will go up, by our calculations, to about 80 percent of insurable acres.

We would also have a standing disaster program, as we have discussed, for all of the crops that are outside of the crop insurance system. This way every farmer has an opportunity to be protected. It is true that we are going to have to couple this with a very strong public education drive to make sure everyone understands

what we have done. To make sure everyone understands that, in fact, the parliamentary barrier is very real and with this type of coverage under the new system, the political push for a disaster bill, would be very much diminished.

The one other point I would make is that you suggested that the parliamentary triple gainer could be done by unanimous consent. One of the reasons that we wanted to push for this was because one thing that has been apparent is that over the past year or so, it seems that every disaster bill that comes up, whether it is for agriculture or for the latest earthquake in California, the level of taxpayer resistance seems to be going up as well. The likelihood a year from now that you would get that triple gainer by consent would be very much diminished.

Senator LUGAR. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. I might add that we are going to be having a hearing on the question of crop insurance specifically, legislation that Senator Kerrey and I and others are going to introduce. Senator Conrad?

Senator CONRAD. Thank you, Mr. Chairman. First of all, let me say, I guess I am going to come at this in a little different way. Anytime I am in a room and everybody is headed in the same direction, I do not know what propels me, but I always kind of want to look the other way. I just look at my own experience. In the 7 years I have been here, we have had 3 disaster years in North Dakota; and I mean extraordinary disasters. In 1988 and 1989, we had the worse drought since the 1930's and it was truly stunning in its impact. Then last year, irony of ironies, we have the 500-year flood. We had in one town in 1 day, 10 inches of rain. They get an average rainfall of 20 inches a year. In 1 day, 10 inches of rain.

North Dakota, as you know, in the eastern part is flat as a pancake. There was nowhere for the water to go. We had extensive flooding. In 1988, we received \$400 million of disaster assistance. In 1989, we received \$120 million of disaster assistance. This year, so far we have received \$104 million of disaster assistance. Without that money, literally thousands of North Dakota farm families would have been forced off the land and there would have been extraordinary economic stress in my State. That is the reality.

These disaster programs have saved people who were damaged by conditions beyond their control. So I think we need to put everything into perspective here.

Abuse is intolerable. It is unacceptable. The message ought to go out, we have zero tolerance for people taking advantage of programs that are designed to save their economic lives in times of catastrophe.

I also think we should put into perspective the magnitude of what we have heard here today. The fact is, this is very small in relation to the size of the disaster programs we have had. Is that not the case?

Mr. ACKERMAN. That is exactly the case and your point is very well taken. These disaster programs have been a very responsible act of Government. They have helped millions of people—farmers, non-farmers—through their darkest hour.

Senator CONRAD. The fact is that during the last disaster assistance program, some several billion dollars worth as a result of

widespread flooding a 500-year flood—the evidence of fraud and abuse, while egregious in several instances, in terms of the totality of the program is relatively minor. Is that not the case?

Mr. BUNTROCK. I think according to what we put together to kind of express it, it is about One and one-fifteenth of 1 percent, or something like that.

Senator CONRAD. One and one-fifteenth of 1 percent. So I think it is very important. I know how the media is. They are going to run out and they are going to write a big headline, abuse of the disaster programs, and they are going to talk about the specific examples in Georgia, and people are going to conclude from that, ah, there it goes again. The Government has a program and they just flush money down the drain and they wasted our money in the middle of that disaster. Well, the true story is, yes, there were examples of abuse. Yes, there are things that are unconscionable, but the larger truth is, 99.8 percent of the money, according to what you are saying here, 99.85 percent of the money, was not abused. It went to save people who were in desperate straits.

I know how the news media is going to report it. They do it the same every time. Everything is the negative. Let us take the negative and put that right at the top of the page. That is what is going to be done. There is nothing about the people who are helped, who are saved from disaster. I drove around North Dakota and water was everywhere. I had a guy bring a picture of his riding a ski doo across his farm field. He had 6 feet of water in his farm field. I can tell you if he had not received \$8,000 of disaster assistance, he would have been out of farming. That is just the reality of how tight things are.

So I hope we do not throw out the baby with the bath water. I must say, based on my experience, I have reservations about where we are going. I really do. Because I know in the crop insurance reform package we are talking about a loss ratio of 1.1, and I will tell you if you look at the recent history of my State we do not meet that, and there is going to be no disaster program. I pray to God we do not have another disaster in North Dakota. We have had three disasters in the last 6 years that are the worse disasters in the cases of drought in 50 years; in flood, the worse disaster in 500 years.

So what can I tell the people that I represent with respect to this program? Are they going to be assured that if there is no disaster program any more, it is going to be virtually impossible to get a disaster program, if God forbid we have another disaster, that they are going to survive economically?

Mr. ACKERMAN. I think the answer is yes and we hope that you will take our program and check the numbers and we think the answer is a very strong yes. We have designed this program to make it clear that if there is a disaster in North Dakota, North Dakotans will be covered. Our critique of the disaster programs is not so much based on the reports of the Inspector General, although they are important, but mostly our concern is about the uncertainty. A farmer in North Dakota suffering a loss next year in a disaster which hits North Dakota and no other State, may face the situation of not having a disaster bill at all.

As far as the 1.1 loss ratio goes, let me be very clear on this. Our loss ratio has been very high over the years. We are required by the reconciliation bill to bring it down. However, it does not govern our payment of indemnities on a year by year basis. For instance, 1993, the year of the flood, for that crop year, our loss ratio is going to be approximately 2.16. Our payment of indemnities comes out of mandatory spending. If we go above a 1.1 loss ratio, we do not by any stretch of the imagination stop paying claims. Claims are paid. Under this program, if there is a disaster in any State and that forces our loss ratio to go above the 1.1, we continue to pay claims, because farmers have paid for them; farmers have bought the insurance; and they are depending on those funds.

Senator CONRAD. I appreciate that. My final point is for these people that took advantage of a situation, I hope they are prosecuted to the full extent of the law. I want to make clear, while I have every sympathy for farmers who have experienced disaster and I have seen it firsthand, the extraordinary economic hardship of drought and flood, these people who take advantage of their neighbors by ripping off programs that were designed to save their economic neck, they ought to be prosecuted to the full extent of the law. You should go after them and after them and after them until you nail them.

Mr. BUNTROCK. If I might just add in that particular case here that, as the Senator has pointed out quite accurately, this is basically in isolated cases where we actually have, to put it mildly, it goes beyond maladministration to the point of criminality in a lot of these cases. That is what we are talking about in the Georgia situation. Unfortunately, in this particular, we had some obvious help or collusion or maladministration by some of the folks in that county. That is why this is so—which seems so obvious when you look at this, and that is why it happened. Those people have been suspended and are under investigation currently.

The CHAIRMAN. I might note that when I met with Mr. Womble, and the others, regarding whether this is an isolated case or not, I think about the first question I asked was, I hope this matter is before a grand jury? I was assured it was. I must admit that my instincts were more of those of a former prosecutor than those of Chairman of the Agriculture Committee. We will do the oversight, because I want to make sure that it is an isolated case. If it is not an isolated case, then we are going to be having a lot of these kind of oversight hearings.

We can do that. We can do everything possible to tighten up the law. Yet, there is no law, as we all know, that is full proof. I mean we have laws against burglary. We have laws against armed robbery and everything else, but people commit the crimes. I think it is incumbent upon us in every single incidence where we find a violation of law, people ought to be prosecuted. We are talking about 18 producers receiving disaster payments totally \$862,000. I mean this is not somebody doing shoplifting. This is real grand theft. We find that county-wide disaster assistance programs based in inaccurate information amount to \$1,300,000.

People run out and say we ought to lock up this kid for stealing a car. It may be a \$5,000 car. We ought to lock up producers or anybody else who steal a million of the taxpayers' money. I get very

concerned that it seems the more you steal, the less chance you have to get a major penalty. You go off and steal \$50 million or a \$100 million or \$200 million, you are only probably going to get a book contract out of it. You get a slap on the wrist and then you will go to prison for a couple of months, find religion, spend part of your ill gotten gains on some shelter for whatever, be claimed a hero and go back home.

Well, these people are just as much criminals as somebody who breaks into a warehouse and steals a much smaller amount. So I think that one of the reasons for this hearing—and I want to commend those from the IG's office who have worked so hard with us in getting this information—is to focus attention on it.

I hope one thing that will happen is that if there are other instances of this in any State, anywhere, that people will pick up the phone, call the hot line, because it is very clear that the administration is willing to send the IG's office down immediately to investigate. So I would hope that if this is covered by the press, and if people hear about it, and you know of such fraud, pick up the phone, call the hot line. If you are concerned about calling there, call me or call Senator Lugar. Call this committee and we will make sure that the word will get back to where it is supposed to. If we are going to have farm programs, if the American taxpayers are going to pay for farm programs, they have to know that the programs are going to the people who deserve it, not going to the rip off artists.

Senator Coverdell?

Senator COVERDELL. Thank you, Mr. Chairman. I will be reasonably brief. I have just come from a town hall meeting in Tifton, very near the locale of this incident. I think something that needs to be said is that the farm communities are in the front of the line in terms of wanting these things to be corrected, they indicated this throughout the hearing—of course, there was already rumor, a substantial rumor and knowledge of the context of this hearing. I heard a term I had not heard before which was called "farming for disaster."

So there is a broad awareness of the problem, at least in our State with regard to these problems and while they may be, as a percentage incidental, they are magnified enough that there is a broad understanding of these kinds of difficulties, and the farm community stands ready to make changes and more, expects these changes to occur quickly as possible.

Just a couple of technical questions. One, the Chairman alluded to the region where this investigation took place. As I understand it, you are making inquiries beyond just these two counties in Georgia?

Mr. BUNTROCK. That is correct.

Senator COVERDELL. Among those farms that spoke during the recent forum in Georgia, I felt a consensus that the ad hoc program needed to be reformed and consolidated. I think the Secretary and you, as representatives in the specifics of it, are headed in an appropriate direction. I think that there is a community belief that this system has come unraveled.

The best evidence you can think of is even if we have an incident of 50 percent participation in your State and only 33 percent nationwide, I think it is about 29 percent in Georgia, there is something not working right. There is a lack of confidence in the system. I might also add that is an oxymoron with regard to the concept of insurance. Insurance does not work when you have incidental participation in it. So I think you are headed in an appropriate direction.

You mentioned under the reform proposal that you would be given authority, I use that word for the first time, to gather pertinent data with regard to crops not in the program. What do you mean by authority?

Mr. BUNTROCK. Basically, Senator, in compliance with the statute, we are required to only collect information from farm producers that is necessary to administer programs. In other words, we do not have authority such as the Statistical Reporting Service who might go out and collect data for crop reporting and so on. We simply do not have explicit authority to gather information and to do things unless it is clearly related to the administration of programs. Now I acknowledge that this is kind of a hazy area where you are talking about these ad hoc programs because we know that sooner or later we are going to be dealing with them.

However, we do not always know the extent to which they will be funded and the crops that they will normally cover. In other words, it has just been recently that the list has grown in terms of those crops that are covered. I guess we have almost got everything now, but the point is that first of all is the uncertainty and how many years you might—if you stop and think about it this way—on a national basis today, we have some form of disaster occurrence in agriculture as we all know somewhere each day, each year.

The fact of the matter is you would have areas of the country who are fortunate enough that they may go several years without that major kind of a disaster where these ad hoc programs would apply. In the interim period we continue to collect this data and information. Now if they were participating up front in an insurance program, even under this basic catastrophic, in that particular case, we would certainly have the requirement and the need and the direction from Congress that we certainly must do that.

Senator COVERDELL. So you are basically talking about your authority to conduct this database accumulation and not necessarily the authority to mandate. The reason I ask the question is because with increasing frequency I run across incidents where the Commerce Department requires businesses to divulge information we used to seek in a voluntary capacity. With more and more frequency you get an envelope in the mail, and the message from the Commerce Department is "You will do this or else." I was curious as to the techniques that would be used to gather the data in which to obtain crop production histories from individual producers.

Mr. BUNTROCK. Let me just very briefly answer here. Now and then I am going to turn to Mr. Ackerman. Basically the 50 crops that crop insurance will continue to cover, I imagine under this

new reorganization that a lot of that information we will be collecting. We also, as you know in the reform package, there is a specific coverage of those crops outside of the 50 that crop insurance covers. Specifically, in this case an area could expect disaster to apply when you hit the 35 percent trigger. It would not be subject to a lot of things that we go through now and subject to an action by Congress. It would be triggered when you reach that threshold. Without that kind of legislation, we would be hard pressed to justify to go out and collect that kind of data without coverage by crop insurance or without anything explicitly in the law. That is what I am referring to.

Now we, basically you also got to remember that a lot of producers who raise specialty crops are not the kind of producers that we see coming to the county offices on a daily basis. Producers who come to that office, we can pick up the additional information from a producer who is involved in program crops. A lot of these specialty crops where there is not a program in effect, the only time we will see them, and we saw of them for the first time, and they saw us for the first time, is the result of disaster.

To go out and seek that information from these individuals who have no other reason to visit that office would require some pretty good justification from the standpoint of the cost of doing it, the standpoint of why it is needed and what you are going to do with it and that sort of thing.

Senator CONRAD. Could I just interject. I had a pretty good squash crop coming before the disaster here in Washington and I was wondering where would I apply for my coverage on that?

Mr. ACKERMAN. Squash is not covered and it is not on our list in the pipeline for many of the reasons cited by the Inspector General. I would just make two very specific points on this record collection under the disaster part of the program, not the insurance part, but the disaster part.

We are putting in the legislation two specific requirements. One is that a producer provide an acreage report at an early date, by a deadline, of how many acres they are planting, even of a specialty crop. That way we will know up front what the exposure is. They will have reported to the local office what they are planting. When you go through the inspector general's report, you can see how that would have avoided a number of the problems that came up in those two counties in Georgia.

The second point is that we base the disaster program, we borrow a concept from crop insurance, we base the disaster program on APH yields, actual production history yields. A producer would have to bring in at least 4 years of production records up through 10 years of production records to establish what their protected yield would be. If they have no records, they would get a yield but it would be at a 35 percent discount. So that would be a very major disincentive to fund the program. It does put a record's requirement on them. They have to show what their production has been in order to get their yield.

The CHAIRMAN. In fact, I think what we might—

Senator COVERDELL. I just have one more quick question, Mr. Chairman, to Mr. Ebbitt. As I understand, you have audited both crop insurance program itself and the disaster ad hoc; is that true?

Mr. EBBITT. Yes, sir, we have.

Senator COVERDELL. What kind of comparison in terms of the degree of abuse can you draw from these two investigations? Is there any parallel?

Mr. EBBITT. There are some parallels in the kinds of problems that we found in both programs. One concern is—how much production is actually out there? On the crop insurance side, we have found instances of where a farmer will insure parcel A and have another parcel maybe across the road or something like that, that is not insured. We found instances where production has been shifted to the parcel across the road in order to take advantage of the parcel that is insured. Those are the kinds of problems, we have typically found.

I do think that with the reinsurance process, the claim's adjustment process, if the claim's adjuster is doing his or her job properly, there are more controls with crop insurance than there have been on the disaster side. It is safe to say that we have identified some problems over time on crop insurance. As the loss ratio would indicate, there have been some problems there.

The CHAIRMAN. In fact, let me go through some of the steps with Mr. Womble on this. Let's look at the sort of things that the ASCS office could look at. Let us assume the crops were planted. How would the ASCS office determine how many pounds of squash would have been produced had there not been a disaster? I mean what do they use for a touchstone?

Mr. WOMBLE. They use information obtained from the National Agricultural Statistics Service of 9,600 pounds of squash per acre.

The CHAIRMAN. That is about what they would normally find if people were growing squash in that area of the country?

Mr. WOMBLE. That is what they had established that they would expect to have been produced, yes, sir, using recommended farming practices.

The CHAIRMAN. Including irrigation?

Mr. WOMBLE. Including irrigation, that was the established rate.

The CHAIRMAN. Actually if you are talking about what the potential for payments would be, the potential would be much higher if you had an irrigated field than if you had a non-irrigated field; is that correct?

Mr. WOMBLE. Normally, yes, sir, the return would be substantially higher for irrigated than for non-irrigated.

The CHAIRMAN. The 9,600 pounds per acre comes from an irrigated field?

Mr. WOMBLE. The 9,600 pounds per acre, as established by the National Agricultural Statistics Service, reflects production, using recommended farming practices to include irrigation.

The CHAIRMAN. I mean that is what the National Agricultural Statistics, if they talk of 9,600, they are talking about an irrigated field, are they not?

Mr. WOMBLE. They establish it as 9,600 pounds per acre and the recommended farming practice for squash requires irrigation, yes, sir.

The CHAIRMAN. We are talking about 4,081 acres on which payments were made. Out of the 4,081 acres, how many were actually irrigated?

Mr. WOMBLE. Only 578 acres were irrigated.

The CHAIRMAN. So even though, what is that 13, 14 percent or so were actually irrigated, the payments were made assuming that they were all irrigated?

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. So you have 4,000 some odd acres and only 570 or so are irrigated, but the payments are made as though 4,000 were irrigated?

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. Now nonprogram farmers get a disaster payment that is based on the market price, but that includes only the planting of it, but they also have to figure out the fact that it cost something to harvest it?

Mr. WOMBLE. Right.

The CHAIRMAN. If you have the disaster before the harvest, you do not have the cost of harvesting it, obviously. What is the difference between the harvest cost and the preharvest cost per acre?

Mr. WOMBLE. The Georgia Cooperative Extension Service put out some estimates showing that the total cost of producing and harvesting an acre of squash was about \$1,500 an acre. The pre-harvest position of that cost was about \$384 an acre.

The CHAIRMAN. Now suppose the squash is being planted but the people have no intention of harvesting it, no intention of doing anything. We have already said the harvest costs would be about \$1,500 per acre.

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. What would it cost per acre if you just wanted to plant it, but you don't have any intention of harvesting it?

Mr. WOMBLE. We estimated those costs would be about \$40 to \$50 an acre.

The CHAIRMAN. Pretty substantial difference from \$1,500 an acre?

Mr. WOMBLE. Yes, sir.

The CHAIRMAN. Why is that? What is the largest part of the cost of harvesting?

Mr. WOMBLE. The labor costs are by far the largest.

The CHAIRMAN. So if you know you are not going to have those labor costs, it is a much lower cost per acre?

Mr. WOMBLE. That is correct, yes, sir.

The CHAIRMAN. So if the disaster payments are based on harvested cost, the U.S. Government paid disaster payments far higher than it could have actually incurred?

Mr. WOMBLE. That is correct.

The CHAIRMAN. I do not want to put words in your mouth, but basically is it, the Government paid farmers for the wages of farm workers which they never hired to harvest crops that they never harvested and may never have planted?

Mr. WOMBLE. Yes, Mr. Chairman, that would be correct in some of the instances we saw.

The CHAIRMAN. Hell of a deal, isn't it?

Mr. WOMBLE. Very much so.

The CHAIRMAN. This is pretty remarkable. I mean this is sort of like developing a perpetual motion machine or figuring out how

to take gold out of—I mean this goes beyond your triple gainer, Mr. Ackerman.

Mr. Gahr, GAO looked at this issue, I believe you have a chart on this, but how does program versus nonprogram disaster payments compare?

Mr. GAHR. Mr. Chairman, there is a certain amount of disparity in program and nonprogram crops. I will call your attention to this chart.¹ The upper chart is a picture of Georgia. On the left-hand side are nonprogram crops. On the right-hand side are program crops. You can see the graph. With disaster payments on nonprogram crops, the producer can achieve up to 190 percent payment of production costs, not including his harvest cost. On program crops, the producer can get up to 60 percent of production costs. There is a big disparity between payments for nonprogram² and program crops.

I have a real world example from our 1991 report. We were in Georgia taking a look at the 1988 and 1989 disaster situation. In 1988, we have a soybean producer who planted 60 acres of beans. The disaster payment that was available, per acre, on 60 acres of beans was around \$60. A total of \$3,600 if his crop had failed. After the 1989 law was passed, this producer shifted to planting 90 acres of squash. The disaster payment on squash is approximately \$1,000 an acre. His crop failed. He received 99 percent of his disaster payment, so he received \$90,000 in disaster payment.

The payment disparity of \$86,400 between the program and the nonprogram crops provides a large incentive for this type of crop shift. That is just one example, Mr. Chairman.

The CHAIRMAN. So in this case that we have been talking about down in Georgia, farmers are paid in one aspect of it, far more than they should have been, because they assumed the land was irrigated when, in fact, we find that most of it was not. Then they were paid the full payments, based on the assumption that they had paid the full cost of harvesting crops when, indeed, they had not. I mean that happened anyway. That even goes before you go to the question whether there was ever a crop there to begin with?

Mr. GAHR. That is correct.

The CHAIRMAN. I mean even if there had been a crop, in most instances it was not irrigated, so it would have cost less. Even if there had been a crop, it was not harvested and my understanding is harvesting is the big part of the cost because it is labor cost. It is fascinating.

Now this goes back to something Mr. Gahr said in his real life example. Let us go back to Mitchell County. There were 400 acres of squash planted in Mitchell County in 1988 before the disaster program. After the disaster program, how many acres of squash?

¹ See chart on page 22.

² GAO Report to Congressional Requesters, *Disaster Assistance, Problems in Administering Payments for Nonprogram Crops*, June 1991; is retained in Committee files.

Figure 4.1: Disaster Payments for Selected Georgia Nonprogram and Program Crops as a Percentage of Production Costs per Acre Prior to Harvesting

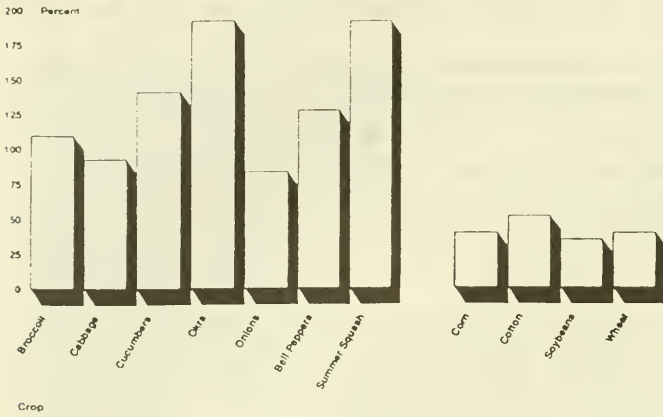
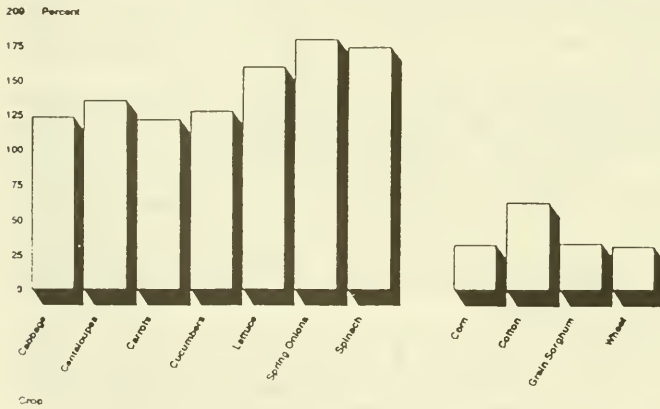


Figure 4.2: Disaster Payments for Selected Southwest Texas Nonprogram and Program Crops as a Percentage of Production Costs per Acre Prior to Harvesting



Note: We used (1) payment rates for fresh rather than processed crops and (2) production costs for irrigated crops.

Mr. WOMBLE. Based on information obtained from the Georgia Cooperative Extension Service, it was estimated that about 10,000 acres were planted in 1992.

The CHAIRMAN. Before that it was 400?

Mr. WOMBLE. Yes, sir, that is correct.

The CHAIRMAN. I never knew there was such a demand for squash. It must be all those kids eating their vegetables. That is a 24, 25-fold increase. Does it appear that the planting was being done more for the program than for the market?

Mr. WOMBLE. Yes, sir, it does. The county executive director in that Mitchell County estimated that without the disaster program, there would only have been about 500 acres of squash planted in 1992.

The CHAIRMAN. In fact, then most of these farmers had no history whatsoever of squash plantings?

Mr. WOMBLE. That is correct.

The CHAIRMAN. So even though it is not normal farming practice to double-crop squash and cucumbers after cotton and peanuts; even though it is not good farming practice to plant squash without irrigation; even though the farmers in large part never planted squash; even though the farmers claimed they had planted 25 times more squash during a disaster year, than in good years, the county office still routinely accepted producer/operator certifications for disaster assistance for this crop?

Mr. WOMBLE. Yes, sir, they did.

The CHAIRMAN. Should not have alarm bells started ringing?

Mr. WOMBLE. There should have been something that identified it, yes, sir.

The CHAIRMAN. Let us go to another step. Not only does it appear that people are being ripped off—I understand both the grand jury and the U.S. Attorney are determining this—but you did have producers who suffered actual losses, producers for whom the program is set up. These producers had actual losses. They had done everything they were suppose to do. They had their certification. They did all the rest.

Mr. BUNTROCK, if money is being diverted to fraudulent claims, what happens to the farmers who have real claims?

Mr. BUNTROCK. Mr. Chairman, when this happens the farmers with legitimate claims are affected. In a recent situation, not the last phase of the disaster programs, but the one before for the 1991–1992 losses. We had based on applications, a factor was used to reduce the amount of eligibility because of the limitation on funding. The impact of this kind of thing, of course, impacts producers across the country, as a result of this. We had a factor, for example, of 50 percent, 50.04 I believe it was, add 1 or 2 percent or 3 or 4 percent on to that particular factor, it has a significant impact to those producers who suffered losses—

The CHAIRMAN. The bottom line is the money is diverted for fraud. There is less money available for the real disasters and those for whom the program was designed?

Mr. BUNTROCK. That is correct.

The CHAIRMAN. Mr. Womble, what was the total amount available for disaster payments for nonprogram crops in Mitchell County in 1990 and 1991?

Mr. WOMBLE. \$4.8 million.

The CHAIRMAN. You discussed a Thomas County produce buyer who reported that he had purchased squash from a number of the Mitchell County producers.

Mr. WOMBLE. That is correct.

The CHAIRMAN. Did the same person who claimed to buy the Mitchell County squash, but had thrown out his records, have other transactions with those Mitchell County growers?

Mr. WOMBLE. Yes, sir. Those growers reported that they, in some instances, also purchased their squash seed from that producer in Thomas County.

The CHAIRMAN. So the same individual that provided the sale invoices also bought the squash seed?

Mr. WOMBLE. That is correct.

The CHAIRMAN. He must have some place where he bought the seeds from. Where did he buy the seeds?

Mr. WOMBLE. He told us that some of the seed were purchased from an individual that he had met at the Atlanta Farmers Market. He said that he purchased 1,000 pounds of seed for \$20,000 and paid for it in \$100 bills.

The CHAIRMAN. Is this sort of common practice, you go off to buy it from somebody who is from Arizona visiting Atlanta to buy seeds and you have 20 grand in \$100 bills in your pocket?

Mr. WOMBLE. I would not believe so, Mr. Chairman.

The CHAIRMAN. Pretty big pockets.

Mr. WOMBLE. Yes, sir, they are.

The CHAIRMAN. So again conveniently no canceled checks?

Mr. WOMBLE. That is correct.

The CHAIRMAN. Did he have even an invoice from the person, a receipt or anything?

Mr. WOMBLE. He presented an invoice, but as it turned out it was written on his own letterhead.

The CHAIRMAN. You are not making this up?

Mr. WOMBLE. No, sir, not at all.

The CHAIRMAN. Did it have a name and address from where the Arizona guy was?

Mr. WOMBLE. It had a name and address of an individual and company from Arizona.

The CHAIRMAN. The obvious question, were you able to find such an individual and company in Arizona?

Mr. WOMBLE. No, sir, we looked but we could not locate either the individual or the company.

The CHAIRMAN. If somebody is writing this for a TV play, they would throw it out as being, you know, too ridiculous. Unfortunately, it is our tax dollars that being lost here. Let us talk about the Thomas County producers own farms. Did he receive any disaster payments?

Mr. WOMBLE. Yes, sir, he did. He, his brother, and his father received disaster payments of \$333,628 in the period 1990, 1991 and 1992.

The CHAIRMAN. Did he have vegetable production?

Mr. WOMBLE. Yes, sir, he reported he grew numerous types of vegetables. We identified that, in fact, he did not report a lot of

production. We identified \$474,000 of production that was not reported to ASCS for those 3 years.

The CHAIRMAN. So even though he said he lost most of his vegetable crop, he had sold about a half a million dollars worth of produce?

Mr. WOMBLE. That is correct.

The CHAIRMAN. Did he get paid in \$100 bills?

Mr. WOMBLE. No, sir.

The CHAIRMAN. Mr. Womble, you are bringing back the memories of a courtroom. You have stated this carefully and understated it, I believe, and I have read all of the background material on this. Like the old Dragnet joke, just the facts, and you have laid them out. Unfortunately, these facts are awfully devastating. I commend you and the IG's office for what you have done.

I think that we are at a point where we have to find some better way of doing this. We cannot lurch from disaster to disaster. I am talking about both the natural disasters and the disasters that are created when all of us have our pockets picked collectively. I think that we have to have a comprehensive crop insurance program.

Mr. Ackerman, I would like to see one that would bring all farmers into a program in which they have a real stake. We have to have enough controls, so we are not paying for phantom farm workers. We cannot have a program where crops are planted, either real or imaginary, designed not for the market, not for consumers, but simply for the disaster payments. We cannot have that.

We also have to have a program so that if people have real losses, they are not going to find the money gone because it has been siphoned off by fraud. I think that this hearing was a start and we can work together on it. Again, I would emphasize that if people do know of such things, pick up the phone. Drop a dime and call us. Call us on these kind of things.

Senator LUGAR?

Senator LUGAR. Mr. Chairman, I just want to commend the chart that we have seen. Your question solicited the response in the last round that indicate in the program crops where there is proper data documentation. Obviously, very different results occur from the nonprogram crops. Without being tedious, just want to get back to the thought that whether the legislation passes as a whole, the sort of job that is needed in the nonprogram crops needs to get done. I am hopeful that we will be able to take it in the comprehensive package as you suggested. I think that is the ideal way.

I am also reassured by Mr. Buntrock's testimony and Mr. Ackerman that many of these reforms are occurring anyway, that the blatant fraud that we have heard about today would be unlikely to occur. Yet, the fact remains, that without this kind of data, the chances are considerable, given vegetable crops or fruit crops or other crops, with which we have not had the same experience in disaster or in insurance; the results are rampant to say the least.

I think that is at least one lesson from the hearing that we all take away, that there is at least a concerted effort on all of our part to regularize the situation, so that there is some equity among farmers. That the people in the program crops are not penalized by the fact that they have a regular system and other folks have an irregular one.

The CHAIRMAN. I totally agree with Senator Lugar on that. Again, I emphasize, we are not going to pass these programs to help the people who really should have the help, if it is all brought into disrepute by those who want to rip it off.

Mr. Gahr, I agree with Senator Lugar. The charts that you've obtained from two different States, Texas and Georgia, show the obvious difference between program and nonprogram crops.

Mr. Ackerman?

Mr. ACKERMAN. I just want to make the point that we are now considering making one very specific change in our legislative proposal, growing out of this hearing and our discussions with the committee staff and on reviewing this report; that is, that our proposal keys the disaster program based on market prices. That is how the current disaster program works. That is the way it has always been done, because market prices are always the more reliable, the more accurate.

Clearly the case has been made very strongly this morning that there can be situations where they are just not appropriate. So we are considering perhaps in the change in the legislation, to allow adjustments to it.

The CHAIRMAN. Also, I think the fact that this is now part of a criminal investigation, ought to send the word very clearly to those who deal with these programs at the local level to be careful. If something looks fishy, it quite well could be. I have to think, not just from the testimony here, but from reading all the reports of this, that alarm bells had to be going off. I mean an awful lot of people in this instance had to know, beyond just the person who called the hot line. A lot of people had to know that it was so far beyond the pale that something was wrong.

Thank you. You have been extremely helpful, the five of you, and I really appreciate the time you have taken here.

Thanks.

[Whereupon, at 11:50 a.m., the committee adjourned, subject to the call of the Chair.]

A P P E N D I X

Grant Buntrock

Mr. Chairman, and Members of the committee, I am Grant Buntrock, Administrator of the Agricultural Stabilization and Conservation Service (ASCS). I appreciate the invitation to discuss issues related to disaster assistance programs.

As you know, these programs have been vital to help millions of farmers who have been hard hit by an unusual series of natural calamities over the past few years. Overall, American agriculture would have been in very rough shape without government assistance to get them through floods, droughts, and cold-weather-induced quality problems.

One of the reasons for these hearings is to provide an oversight of payments on specialty crops. As you know, specialty crops, while a small segment of the overall crop disaster program, have been the most difficult aspect of the disaster assistance programs to administer.

As you know many of the abuses outlined in the Office of the Inspector General audits occurred prior to our involvement and, like you, we are very concerned by the level of duplicity shown in some of these cases. Clearly, we do not condone nor will we tolerate such wanton abuse of taxpayer dollars and this administration has already taken steps to assure it doesn't happen again.

Over the years, our agency's expertise has been concentrated on the major program commodities of feed grains, food grains, cotton, tobacco, and peanuts. Our data on these commodities is very good. Such was not the case, however, on the myriad of ornamental and nursery crops included in these programs. Amounts paid, by specialty crop, have ranged from a total of \$2.00 for a hydrangea shrub to over \$11 million for mixed hay, over \$16 million for alfalfa, and nearly \$14 million for watermelons.

In the most recent crop disaster programs dealing with the 1990 through 1993 crops, nearly \$4 billion has been paid to 1.7 million producers to partially reimburse them for crop losses they suffered. Of those totals, \$276 million represented payments to 223,000 producers of specialty crops. The number of different specialty crops on which payments were made reached nearly 1,600. We were amazed at how many specialty crops are actually produced in this country.

You have heard from the General Accounting Office (GAO) and the Office of Inspector General (OIG) concerning audits those agencies conducted on disaster assistance for producers of specialty crops. Auditors have questioned whether improper yields and/or rates were established by county ASC committees for use as a basis for making disaster payments. They also cited cases where it did not appear that adequate production evidence was furnished by producers for losses, causing excess erroneous payments to producers. Solid information is usually available on rates and yields from the National Agricultural Statistics Service (NASS), Extension Service (ES), and State universities for the major commodities. However, on many specialty crops, there have been few benchmarks for guidance.

I should note that of the 11 audits by OIG on specialty crops, less than 15 one hundredths of 1 percent of our total disaster program payments are being questioned. While we recognize no errors in payments should ever occur, administering programs becomes a real challenge when thousands of judgments and common sense

decisions must substitute for records and other evidence often destroyed by the various disasters.

As we consider methods to improve administration of these programs, Mr. Chairman, I would be remiss if I did not mention the administration's aggressive effort to overhaul both the crop insurance and disaster assistance programs. These plans would replace ad hoc disaster programs with an expanded program of crop insurance that farmers can count on when they need it. The reform package would provide all producers of insurable crops coverage for a nominal processing fee—which could be waived for those with limited resources.

I must also commend the overall superb work that has been performed by ASCS county office employees and ASC committees in rapidly responding to critical needs of people who were in desperate situations. The vast majority of those producers whose crop was totally wiped out in last year's Midwest floods, for example, had their crop loss payment check in hand within 2 weeks of the time application was made. This fast turn-around was at the specific request of Secretary Espy and we consider the work our people did to be public service in the finest sense. I should add that on the crop loss payments, for the major commodities, there have been very few complaints about our service, or hints of program abuse. We are very proud of our record, and I commend the thousands of people at the county level who are the unsung heroes. They are the ones who made it work.

Problems we have encountered with specialty crops do emphasize, however, that improvements must be made. We are working with OIG to identify specific problems and taking corrective actions. To keep as current on the issues as possible, ASCS and the Federal Crop Insurance Corporation (FCIC), recently initiated a pilot project to jointly review 1993 specialty crop disaster payments in five States—California, Florida, Louisiana, Missouri, and North Dakota. This is part of our ongoing efforts in improving quality control on these new specialty crop programs. We have, for example issued approximately 26 directives, strengthened procedure no less than 13 times, and provided counties ASCS offices with a number of tools to assist in administration of the disaster programs. Quality control actions include.

- Data queries have been developed to run validity checks and cross-checks on disaster data recorded throughout ASCS files, including electronic data recorded in other files such as payment limitations and producer shares.

- ASCS County Office Reviewers (CORs) have been assigned to perform special reviews in over 200 county offices. The CORs review and verify rates, yields, crop tables, codes production data, applications and other information pertinent to the disaster program.

- Yields, rates, check corrections, and additional payment approvals are now being cleared through Washington, DC.

- County ASC Committees were given more flexibility to make downward adjustments in yields were a portion of the reduced yield was attributable to the producer's farming practices rather than the disaster itself.

Procedures were issued to require that when seed companies pay a disaster-affected grower for his full production, the credit would be considered actual production, and not eligible for disaster assistance.

A joint effort was initiated on a pilot basis between ASCS and FCIC to share some disaster data common to both agencies and to identify areas where abuses are most likely.

We also invite your attention to the proposal submitted by Secretary Espy for reform of crop insurance and disaster programs. That reform proposal provides for ongoing management controls which include establishment of baseline yields; an ongoing acreage reporting system which will include acreage reporting data; and commodity price data.

By administering the crop insurance program, on a permanent basis, we can design a compliance program that will monitor for program abuses and system weaknesses. This will be part of the proposed Info-Share program that will link offices and facilitate quality control systems to detect problems far more quickly than is now possible.

To carry out this mission, a single new agency—the Farm Service Agency—would merge Federal Crop Insurance's risk management programs, FmHA's farm credit programs, ASCS's commodity, and emergency assistance programs. We believe these are extremely exciting proposals which could result in greatly improved services to farmers, I look forward in the months ahead to working closely with you on these promising proposals. I would be happy to take any questions at this time.

James R. Ebbitt

Mr. Chairman, and Members of the committee, I am pleased to appear today to discuss with you both our past, and present audit work of ASCS disaster programs.³ With me today is Charlie Womble, supervisory auditor, Southeast region, Atlanta, Georgia. Mr. Womble will discuss the specifics of what we found in Georgia. I would like to take just a moment to discuss in more general terms work on the disaster program.

Since April 1, 1990, we have issued 29 audit reports dealing with ASCS disaster assistance. Most of the problems we have noted have been in nonprogram crops. These reports have contained a number of recommendations dealing with ways to strengthen the program. ASCS has been cooperative in implementing our recommendations and has been receptive of any recommendation that will help improve program integrity.

Of primary importance is the establishment of realistic production yields and payment rates. Although there is still a need for improvement, ASCS has changed its methods for the establishment of yields and rates by utilizing other sources of information such as NASS and Extension Service. They have also established different rates and yields for crops marketed for fresh versus processing or juice, and for classes of a crop that warrant separate treatment (*i.e.*, red kidney beans versus navy beans). We also identified problems with the implementation of quality loss provisions for the 1993 crops, and ASCS took immediate corrective action that resulted in loss payments that better represented the producers actual loss due to low quality production.

Our reviews of problems in Georgia were initiated when OIG received a whistle blower complaint alleging that producers were planting certain crops, primarily squash, with no intention of harvesting a crop. ASCS requested our assistance in reviewing the allegations. The overall review has been a joint effort between OIG and ASCS. ASCS has taken tough actions where warranted including administrative action regarding two county office employees, one county committee chairperson, and one county committee member.

We are also performing audits of the 1993 Disaster Assistance Programs in about 20 States and 40 counties. This audit now in process is primarily directed towards nonprogram crops, since past audits have revealed larger problems with nonprogram crops as I noted earlier. This audit is also designed to determine if producers that also have FCIC coverage or have requested the same loss information in these programs as they did to ASCS. ASCS has been very cooperative in this major effort.

Mr. Chairman, this concludes my brief statement, and I, or Charlie Womble will be happy to respond to any questions.

William E. Gahr

Mr. Chairman, and Members of the committee, we are pleased to participate in this hearing on initiatives to reform the disaster assistance and Federal crop insurance programs. Our testimony focuses on the difficulties the U.S. Department of Agriculture (USDA) has faced in administering disaster assistance and in ensuring that disaster assistance payments, combined with crop insurance payments, do not exceed legislative limits. We will also provide information on actions USDA and the Congress could take to improve the administration of disaster assistance payments, and better integrate disaster assistance, and crop insurance payments.

Our statement today is based on our 1991 report on USDA's effectiveness in administering the 1988 and 1989 disaster assistance programs and our ongoing work for this Committee on USDA's crop insurance program. (See Related GAO Products.)

In summary, our work to date indicates the following:

- USDA has faced difficulties in administering disaster assistance for nonprogram crops, such as fruits and vegetables. USDA does not have the data it needs to ensure the correct level of disaster assistance payments for these crops. Without good data, overpayments do occur; and when they are discovered, USDA is limited by law (except for fraud or egregious error) to initiating collections on them within 90 days of the original payment determination.

³The *Agricultural Stabilization and Conservation Service Disaster Program—Nonprogram Crops, Crop-Years 1990–1992*, Thomas County, Georgia, Audit Report No. 03099–148—At is retained in Committee files; aforementioned subject matter for crop years 1990–92, Mitchell County, Georgia, Audit Report No. 03097–2—At is also retained.

— USDA has not ensured that (1) recipients of disaster payments for all crops in one year purchase crop insurance the following year, as required by law, and (2) disaster payments made to holders of crop insurance policies are within legislative limits.

As we have previously recommended, the Congress and USDA could take several actions that would improve the administration of disaster assistance payments, ensure that disaster assistance and crop insurance program payments do not exceed legislative limits, and better manage the government's expenses associated with the risks of crop production.

Disaster Payments and Crop Insurance Programs were designed to help producers handle production risks

Because farming is a risky business, the Congress has two principal programs to compensate for weather-related crop losses—ad hoc disaster payments and crop insurance. Between 1988 and 1993, in ad hoc pieces of legislation, the Congress created seven nonpermanent disaster assistance programs. Over this period, USDA paid producers about \$8.8 billion. About 75 percent of this assistance, \$6.5 billion, went to producers of program crops, and another 25 percent, \$2.3 billion, was paid to producers of nonprogram crops—crops that are not eligible for Federal price and income support assistance. For producers of nonprogram crops, 1988 was the first year in which the Federal government made a major effort to provide substantial financial disaster assistance. (See app. I.)

For each successive disaster assistance program, eligibility requirements and payment levels varied, contributing to the complexity of the programs. For example, to qualify for disaster assistance, producers needed to lose 35 percent of a crop in 1988 but more than 50 percent in 1989. In 1990 through 1993, the amount of crop loss necessary to be eligible for disaster assistance payments depended on whether or not the producer had crop insurance. Producers without crop insurance needed losses greater than 40 percent, and producers with crop insurance needed losses greater than 35 percent. Moreover, disaster assistance payments covered more than 1,200 crops and aquaculture, with the basis for the yields and prices used to calculate the payments varying by crops and species. (The prices are set in the disaster assistance legislation. See app. II.)

Disaster payments have occurred despite congressional efforts in 1980 to make crop insurance the preeminent means for providing agriculture disaster assistance. Disaster payments have been utilized because crop insurance has never attained the level of participation the Congress believed necessary to safeguard producers from weather-related risk. The Federal Crop Insurance Corporation (FCIC), within USDA, estimates that it offers insurance on about 75 percent of the approximately \$92 billion in annual commodity production. However, participation has not exceeded 40 percent of eligible acres. Between 1981 and 1993, the Federal government paid \$8.2 billion (61 percent) of the \$13.5 billion cost of the crop insurance program, with producers paying the balance through their crop insurance premiums.

USDA lacks the data it needs to administer disaster assistance for nonprogram crops

In 1991, we reported that USDA had no assurance that the \$1.3 billion paid in disaster benefits for nonprogram crops in 1988 and 1989 were protected from fraud, waste, and abuse. This lack of assurance occurred because of problems in verifying producers' losses and USDA's lack of historical yield and price data. In addition, we found that many disaster payments greatly exceeded producers' actual production costs.⁴

The 1988 and 1989 payments for nonprogram crops resulted from ad hoc disaster assistance programs, and USDA did not routinely collect data on many of these crops. Therefore, the Department was unable to ensure the validity of much of the data producers provided. USDA could not collect crop loss data from producers of nonprogram crops until after the disaster assistance legislation was enacted in August of each year, and the producers had filed their loss claims. The delayed authority resulted in USDA's being unable to verify the validity and accuracy of much of the producers' crop loss data, since evidence had generally been harvested and sold, or plowed under and destroyed.

We also reported that USDA had no assurance that the information it used to compute disaster assistance payments for nonprogram crops was reliable. Disaster legislation requires that such information be based on the 5-year average historical

⁴ As the administrator of the agency—the Agricultural Stabilization and Conservation Service (ASCS)—that paid program benefits pointed out in 1992, it is difficult to ensure the integrity of payments.

price received for crops (payment rate) and average production (yield) over 5 years. This information was not available for many nonprogram crops for which USDA did not routinely collect data. Therefore, in the four States we reviewed, USDA had to establish about two-thirds of its rates and yields using something less than desired historical data. For example, on the basis of 1 year of a producer's data, a Wisconsin field office paid \$500 per ton for watermelons for 1988 crop losses. However, for the 1989 program, the same office used 5 years of data from field offices in three neighboring States and paid only \$300 per ton—a 40-percent reduction from the prior year.

Finally, we reported that USDA paid producers of many nonprogram crops excessively high disaster assistance benefits. This occurred because USDA was required by law to set payment rates based on market prices, without adjusting the payments downward to reflect production costs not incurred. For 14 major nonprogram crops we reviewed in Georgia and Texas, producers received financial assistance ranging from 80 percent to over 190 percent of state extension service estimates of costs incurred prior to harvest. In Georgia, for example, producers of okra and summer squash (nonprogram crops) who did not harvest their crop received disaster payments that were twice their expenses.

After our 1991 report was issued, USDA initiated action to collect overpayments we had reported. However, USDA subsequently determined that a provision in the 1990 farm bill prohibited the agency from initiating action to collect overpayments more than 90 days, unless otherwise appealed, after a payment decision was made—except for fraud or egregious error. Because many of the overpayments we found resulted from administrative difficulties—USDA did not have adequate and timely information on which to base its payments—USDA cannot take action to collect on these overpayments after 90 days. In the four States we reviewed, this restriction means that USDA may not be able to collect overpayments of about \$575,000. This restriction also affects USDA's ability to collect similar overpayments identified by the Office of the Inspector General in its work.

USDA has not ensured that disaster assistance recipients meet requirements for purchase of crop insurance and payment limits

The combined outlays for disaster assistance and crop insurance payments can be significant. For example, for crop years 1990 to 1992, about 50 percent (\$656 million), of the \$1.3 billion in disaster assistance payments in counties where crop insurance was available, went to recipients who purchased crop insurance. (See app. III.) Therefore, agency oversight to ensure that government payments do not exceed requirements is critical for both programs. However, in our ongoing work for this committee, we have noted two areas in which USDA needs to improve its oversight over disaster payments to crop insurance recipients.

First, USDA's procedures to ensure that producers' combined crop insurance and disaster assistance payments do not exceed 5 legislatively set limits are inadequate. The disaster assistance legislation provides that producers' disaster assistance payments, when combined with crop insurance payments, cannot exceed an amount equal to the legislated price multiplied by producers' production yield for each crop. To achieve this objective, USDA is required to obtain from producers the amount of their crop insurance payments, but not any supporting documentation. Representatives of two USDA county offices told us that while one office obtained pertinent documentation from producers, the other did not. Without routinely requiring documentation supporting the amount of the crop insurance payment, USDA cannot ensure that disaster assistance payments do not exceed the limit.

Second, USDA does not effectively monitor the legislative requirement that producers who received disaster assistance payments for losses in one year purchase crop insurance the following year. For 1992 and 1993, the disaster assistance legislation required that producers who were paid for losses of greater than 65 percent for a crop, purchase crop insurance the following year (for that crop on that farm). For 1992, 83 percent of the disaster payments met this loss criteria, indicating that most producer should have purchased crop insurance the following year. To get a preliminary indication of whether this was the case, we spoke with representatives of two county offices. They told us that USDA requires county offices to inform disaster payment recipients of this requirement; however, USDA does not require the verification of this purchase. In response to our questions on this issue, USDA recently initiated an effort with FCIC to verify that producers who were required to purchase insurance did so.

Changes in the administration and structure of disaster assistance and crop insurance could better manage Government costs

Since the early 1980s, we have reported on problems in the administration of both the disaster assistance and crop insurance programs and recommended structural changes to both programs to better manage government costs. Two recommendations we made are relevant to your hearings today. First, we believe that USDA needs data on nonprogram crops to ensure that disaster assistance payments for those crops are appropriate. Without legislation, USDA cannot put into place the necessary data collection effort that would ensure payment integrity. Such data could be collected by USDA or required of producers. Second, we have asked the Congress to consider integrating crop insurance and disaster assistance programs to improve risk management, reduce administrative costs, improve equity to all farmers, and encourage complementary public-private risk enterprises.

Conclusions

The difficulties in administering ad hoc disaster payments and crop insurance indicate the need to develop a more effective approach to providing risk management alternatives to producers. We believe that integrating disaster assistance and crop insurance programs could assure producers of continuous disaster coverage. At the same time, this integrated program, if properly designed and implemented, could better protect government funds.

This concludes my prepared testimony, Mr. Chairman. We would be pleased to answer any questions you or Members of the committee may have.

DISASTER ASSISTANCE PAYMENTS TO PRODUCERS BY TYPE CROP
AND AVAILABILITY OF CROP INSURANCE, CROP YEARS 1988-93

Type crop and crop year	Payment type and availability		Total number of producers
	Income support only	Price support only	
Income support only crops			
1988	1,000,000	1,000,000	1,000,000
1989	1,000,000	1,000,000	1,000,000
1990	1,000,000	1,000,000	1,000,000
1991	1,000,000	1,000,000	1,000,000
1992	1,000,000	1,000,000	1,000,000
1993	1,000,000	1,000,000	1,000,000
Subtotal	6,000,000	6,000,000	6,000,000
Price support only crops			
1988	1,000,000	1,000,000	1,000,000
1989	1,000,000	1,000,000	1,000,000
1990	1,000,000	1,000,000	1,000,000
1991	1,000,000	1,000,000	1,000,000
1992	1,000,000	1,000,000	1,000,000
1993	1,000,000	1,000,000	1,000,000
Subtotal	6,000,000	6,000,000	6,000,000
Nonprogram crops--insurance offered			
1988	1,000,000	1,000,000	1,000,000
1989	1,000,000	1,000,000	1,000,000
1990	1,000,000	1,000,000	1,000,000
1991	1,000,000	1,000,000	1,000,000
1992	1,000,000	1,000,000	1,000,000
1993	1,000,000	1,000,000	1,000,000
Subtotal	6,000,000	6,000,000	6,000,000
Nonprogram crops--insurance not offered			
1988	1,000,000	1,000,000	1,000,000
1989	1,000,000	1,000,000	1,000,000
1990	1,000,000	1,000,000	1,000,000
1991	1,000,000	1,000,000	1,000,000
1992	1,000,000	1,000,000	1,000,000
1993	1,000,000	1,000,000	1,000,000
Subtotal	6,000,000	6,000,000	6,000,000
Total	24,000,000	24,000,000	24,000,000

Note: Program crops includes both the crops for which income and price support are available and crops for which only price supports are available. Income and price support crops are barley, corn, grain sorghum, oats, rice, upland cotton, and wheat. Crops just receiving price support are ELS cotton, oilseed (soybean, flax, mustard, rapeseed, sunflower, sesame, soybeans, and sunflower seed), honey, peanuts, rice, sugar beets, sugar cane, and tobacco.

Source: GAO analyses of ASCS and FCIC data. To do this analysis we needed to link ASCS's computer files that showed payments on 1,265 crops and first with FCIC's computer files that showed 51 major crops. To do this, FCIC matched the 51 major crops with about 400 crops in ASCS's records.

APPENDIX II

APPENDIX II

DISASTER ASSISTANCE PROGRAM PROVISIONS
FOR YIELDS AND PRICES, CROP YEARS 1990-93

Crop Category	Yield	Price
Participating program crops and ELS cotton	ASCS yield	65 percent of target price.
Nonparticipating program crops and ELS cotton	ASCS yield	65 percent of loan rate.
Sugar beets and sugarcane	County average yield	65% of price support level
Peanuts	Farm yield	
Quota tobacco	County average yield	
Soybeans, sunflowers, and nonquota tobacco	County average yield	65 percent of 5-year average price, dropping highest and lowest years.
Nonprogram crops	County average or proven yield	

Note: For 1990-92, a budget factor of 50.04 percent was applied to the payments calculated, reducing the payments by about one-half.

DISASTER ASSISTANCE PAYMENTS TO PRODUCERS WHO HAD
CROP INSURANCE AVAILABLE, CROP YEARS 1990-1992

Type crop and crop year	Payments to producers who		Total payments
	Purchased crop insurance	Did not purchase crop insurance	
Income and price support crops			
1990	\$93,709,687	\$44,915,336	\$138,625,023
1991	159,634,182	145,218,615	304,852,797
1992	228,579,501	162,956,421	411,535,922
Subtotal	481,923,370	373,090,372	855,013,742
Price support crops only			
1990	48,594,165	\$31,045,168	79,639,332
1991	38,838,517	54,979,968	93,818,485
1992	22,165,240	23,703,318	45,868,558
Subtotal	109,597,922	109,728,453	219,326,375
Nonprogram crops			
1990	27,181,629	\$60,868,062	88,049,691
1991	17,443,433	34,597,851	52,041,284
1992	19,457,795	39,015,167	58,472,962
Subtotal	64,082,857	134,481,081	198,563,938
Total	\$655,604,149	\$617,300,106	\$1,272,904,255

Note: Program crops includes both the crops for which income and price supports are available and crops for which only price supports are available. Income and price support crops are barley, corn, grain sorghum, oats, rice, upland cotton, and wheat. Crops receiving only price support are ELS cotton, oilseeds (canola, crambe, flax, mustard, rapeseed, safflower, sesame, soybeans, and sunflower seed), honey, peanuts, rye, sugar beets, sugar cane, and tobacco.

Source: GAO analysis of ASCS centralized computer accounting records (1) showing payments on about 400 ASCS crops for which FCIC offered insurance and (2) showing whether the producers had crop insurance. Information for payments in 1988-89 was not readily available in the format needed for this analysis and for 1993 was not yet available on the centralized records.

RELATED GAO PRODUCTS

Management Reform: GAO's Comments on the National Performance Review's Recommendations (GAO-OGC-94-1, Dec. 3, 1993)

Crop Insurance: Federal Program Faces Insurability and Design Problems (GAO-RCED-93-98, May 24, 1993)

Crop Insurance: Program has not Fostered Significant Risk Sharing by Insurance Companies (GAO-RCED-92-25, Jan. 13, 1992)

Disaster Assistance: Problems in Administering Payments for nonprogram Crops (GAO-RCED-91-137, June 28, 1991)

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SENATOR LEAHY'S QUESTIONS FOR WITNESSES
AND THEIR RESPONSES THERETO

James R. Ebbitt

The Chairman: Mr. Ebbitt, during the hearing held on April 13, 1994, it was agreed that approximately 99.5 percent of the disaster payments are properly received.

Mr. Ebbitt: Mr. Chairman, we did not agree that only 99.5 percent of the total disaster payments were in error. This matter was discussed between ASCS and a member of your committee. The 99.5 percent was apparently derived from OIG having identified about \$3 million of exceptions in our disaster audits and comparing that amount to total disaster payments. However, we only audited a total of \$5.6 million in disaster payments to producers of nonprogram crops. The \$3 million in erroneous payments can not be compared against total disaster payments to establish an error rate.

Question 1. What percentage of the disaster payments would you estimate are made based on inaccurate claims?

Answer. We cannot say what percent of error exists in the total disaster payments already made because our sample was judgmentally selected. Based upon our judgmental sample of 1990 and 1991 disaster payments made on nonprogram crops, the error rate was about 34 percent for those producers we reviewed who received disaster assistance for nonprogram crops. However, the exceptions totaled about 53.6 percent of the dollars included in our sample. However, I again stress that, because we judgmentally selected these producers, this error rate applies only to the cases we reviewed. Nonprogram crops represent between 20 and 30 percent of the total disaster assistance program.

Question 2. What is the basis for your estimate?

Answer. Our estimate is based upon a judgmental sample of 231 producers that received about \$5.6 million in disaster assistance on nonprogram crops in 5 States in 1990 and 1991. Of this total, 79 producers had received about \$3 million in questionable payments. However, 37 of these producers, receiving about \$2 million in questionable payments, were in two counties in one State that we audited because of a whistle blower complaint.

Question 3. How does this relate to the total universe of the disaster payments involved in your audits conducted within the last 2 years?

Answer. The total 1990 and 1991 disaster assistance paid on nonprogram crops reviewed in these 5 States was about \$57 million. Our total review sample was about 9.8 percent of the \$57 million paid in these States. Our exceptions represented about 5.3 percent of the \$57 million.

Question 4. How does this relate to the total amount of disaster payments made nationwide?

Answer. The total 1990 and 1991 disaster assistance paid on selected nonprogram crops (e.g., spinach, cantaloupes, squash, etc.), which constituted our audit universe, was about \$153 million. The universe in the 5 States we reviewed represented about 37.2 percent of this total. Total funds appropriated for disaster payments provided \$995 million to producers for losses in either 1990 or 1991 crops, at the producer's option. Also \$755 million was made available by request of the President on September 2, 1992, for disaster payments on 1990, 1991, and 1992 crops.

Question 5. What percentage of those payments were questionable?

Answer. We can not say at this time what percentage of the total disaster payments made were questionable.

Question 6. What remedies are available to prevent such questionable payments in the future and recover past payments?

Answer. For the future, questionable payments can be prevented by requiring ASCS to verify items reported by producers of nonprogram crops (i.e. production and crop shares) to insure that producers had not made false certifications. If false certifications are found, ASCS needs to require repayment by the producer and/or seek criminal prosecution. However, the "90-day rule" prevents collections if misrepresentation is not involved. The 90-day rule was legislated in the 1990 Farm Bill and prevents the collection of erroneous payments to producers resulting from county committee error, or a representative of the county committee, once 90 days from the date of payment has passed.

To prevent future errors the following could be done:

- Legislation that would require (1) producers of nonprogram crops to report planted acres annually at the time of planting to ASCS; (2) payments be representative of the cost the producer has in the crop (*i.e.*, lower payments if crop is not harvested or planted); (3) individual yields and rates (especially for those crops with limited production) be based upon individual producer's verifiable history; (4) disaster designations and corresponding sign ups be more timely (*i.e.*, in year of loss), however, the *ad hoc* nature of disaster assistance may be eliminated by the current legislative efforts; and (5) producers found to have provided false information be subject to penalties such as the Program Fraud Civil Remedies Act.

- ASCS needs to establish better controls, such as (1) requiring producers to provide copies of production contracts, (2) verifying producers income if the current \$2 million limitation is maintained, (3) more timely and reasonable spot checks of producers, these spot checks need to include verification of producers' reported production, (4) verification of planting dates etc. by the county committees when approving applications for disaster credit, and (5) ASCS employees and committees being held responsible for their actions in the administration of the program.

Grant Buntrock

Question 1. How can we be assured that this is not occurring in those locations not reviewed by OIG and that the percentages are as low as presented at the hearing?

Answer. In addition to the tools provided to State and county Agricultural Stabilization and Conservation Service (ASCS) offices by way of the quality control actions noted in my statement to the Committee, we have provided our State Executive Directors (SED) and State Agricultural stabilization and Conservation Committee's (STC) with the latitude to direct county off ice reviews (COR) or special field reviews to ensure that proper procedures are followed in the delivery of our programs, including disaster programs. CORs and special reviews are part of the County Office Review Program which was established with the assistance of Office of Inspector General (OIG). CORs are conducted on county ASCS office administration of programs, and special reviews are conducted by State ASCS office program specialists on specific program activities, *e.g.* the Disaster Assistance Program. As an example, when the joint OIG for Audit and ASCS task force reviewed Mitchell and Thomas County ASCS Offices in Georgia to identify the extent of the problem with the administration of the disaster program for nonprogram Crops in these two counties, additional special program reviews were also conducted in three adjoining counties. Although these additional reviews identified minor errors, they revealed no significant problems in the administration of the Disaster Assistance Program.

It is through the use of normal CORs, special program reviews, and joint task force operations with OIG and, more recently with the Federal Crop Insurance Corporation, that reasonable assurance can be given that these cases cited in Mitchell and Thomas Counties are isolated cases. Our State ASCS Offices continue to monitor the pattern of disaster applications and the payments to individual producers to determine if irregularities exist to ensure early detection of problems in the Disaster Assistance Program.

Question 2. Are there any penalties assessed when a producer knowingly submits fraudulent documentation for disaster payments as in the incidents found by OIG auditors in both Mitchell and Thomas Counties in Georgia?

Answer. There is no legislative authority for ASCS or Commodity Credit Corporation (CCC) to administratively assess penalties against producers participating in the ASCS/CCC Disaster Assistance Program such as those found in the legislative authority for the tobacco and peanut programs. However, we do ensure that we take all applicable administrative actions within the limits of the law to recover payments from producers who are found to be ineligible for such payments. These actions include administrative offset and the filing of civil actions to recover payments.

Question 3. Is the Program Fraud Civil Remedies Act (PFCRA) applicable to the Disaster Assistance Program?

Answer. The PFCRA establishes a procedure for the investigation and processing Of potential fraud claims which could be applied in the fraud cases that involve the Disaster Assistance Programs. Pursuant to the provisions of the CCC Charter Act,

as amended, we have established with OIG a series of procedures regarding the investigation and referral for prosecution of potential fraud matters. The establishment of these procedures in most cases predates the enactment of the PFCRA; however, we believe that these procedures regarding the referral of potential fraud cases to OIG for investigation are consistent with the requirements of PFCRA, regardless whether this Act is specifically involved in such referrals.

Question 4. Is the PFCRA invoked for any of your other programs where abuse occurs but no criminal actions are being pursued?

Answer. OIG has already discussed with us the possibility of criminal prosecution with the U.S. Attorney's Office upon completion of OIG investigations. In cases where there is no criminal prosecution, an examination will be made regarding the possibility of a civil prosecution or the establishment of administrative claims. Again, we believe that this process is consistent with the intent of the PFCRA.

Question 5. Does ASCS have a tracking system in place to monitor payments which are not repaid as a result of the 90-day rule?

Answer. ASCS does have a tracking system in place to monitor payments made as a result of actions taken under the statutory 90-day rule provisions.

Question 6. What percentage of these payments are caused by employee errors versus inaccurate data being provided by the producers?

Answer. In accordance with the statutory provisions governing the 90-day rule, 100 percent of these cases are the result of some error by an employee or other ASCS representative. If the erroneous payment was solely the result of a producer providing inaccurate data, the collection of such payment would not be restricted by the 90-day rule, because the producer did not act in good faith. If however, the producer presented inaccurate data because of misinformation provided by our employee or representative, then it is possible that recovery of the payment would be restricted by the 90-day rule.

BLUEPRINT FOR FINANCIAL SOUNDNESS

SCOPE AND PURPOSE

The Omnibus Budget Reconciliation Act of 1993 (OBRA 93) contains provisions concerning the Federal Crop Insurance Program. These provisions direct the Federal Crop Insurance Corporation (FCIC) to take steps necessary to improve actuarial soundness of the Federal Crop Insurance Program and to achieve, by the fiscal year beginning October 1, 1995, a projected overall loss ratio not to exceed 1.10 (110 percent) (section 1501 (a)).

Projected loss ratio (dollar amount of losses paid as a percent of the total premiums collected) is intended to be a performance standard, not an absolute ceiling for the operations of any particular crop year. Congress recognizes that adverse weather conditions (such as extreme drought or flood) will influence the financial results of each year's operations; however, when good and poor years are averaged over a long period of time (such as 50 to 100 years), the expectation must be that the program will operate with an average loss ratio of 1.10 or less. A period of time at least this long is needed to observe a range of production conditions that are likely to be encountered by farmers. Short time periods, such as to 10 years, may encompass several favorable or unfavorable years, the frequency of which is atypical of the longer term. This is a primary reason that the risks covered by the Federal Crop Insurance Program cannot be financed in a commercial insurance environment.

OBRA 93 directed FCIC to take the following actions to achieve this required improvement in the loss ratio:

- Institute rules for producers to demonstrate actual production histories in establishing yields for Federal crop insurance coverage that better reflect the associated actuarial risks.
- Establish in appropriate counties an optional "area yield" or "group risk" plan that allows producers to qualify for an indemnity if a loss occurs in a specified area in which the producer's farm is located.
- Create a nationwide database to track producer participation using social security account and employer identification numbers. Such a tracking system would facilitate better production documentation, high-risk producer identification, and assessment of insurance providers' performance.

- Take other measures authorized by law to improve the actuarial soundness of the Federal Crop Insurance Program while maintaining fair and effective coverage for producers.

FCIC is committed to achieving these actions because it is good public policy. A financially sound program is essential to maintaining public confidence in crop insurance. Sound management to achieve these actions will promote long-term stability of the program and facilitate the overall economic stability of the United States agricultural sector. Crop insurance differs from commercial insurance because it serves social goals, not solely the business objective of maximizing profit. A stable crop insurance system never developed in the private sector without government support because of the unique and widespread risks inherent in farming.

Section 1501(c)(2) further directed the Department to issue for public comment a comprehensive plan or "blueprint" that identifies, among other things:

- Steps FCIC intends to take to achieve a projected overall loss ratio of no greater than 1.10 on and after October 1, 1995.
- Additional steps if further action is required, based upon actual program experience or unforeseen external circumstances.
- Modifications to be considered if initial actions to improve actuarial soundness work better than anticipated.
- Projections, assumptions, and analyses which underlie the FCIC conclusions that the above actions will achieve the required loss ratio within the stated deadline while maintaining fairness and effective coverage to agricultural producers, and which thereby demonstrate FCIC's compliance with the performance standard identified in section 1501(a).

This document proposes a draft comprehensive Blueprint for Financial Soundness, as required by OBRA 93 for discussion and public comment. The plan has been developed with the guidance of various persons involved with crop insurance (producers, insurers, agents, academics, and others). The plan will be modified periodically to incorporate resulting analyses of program performance and the recommendations of interested parties as required by OBRA 93.

Actions identified herein result from internal analysis by FCIC and information previously provided to FCIC by numerous interested parties. These include the Commission for the Improvement of Crop Insurance (a Congressionally established work group in 1989 and 1990), various crop insurance industry organizations, members of Congress, agricultural producers, crop insurance agents and insurance companies, the General Accounting Office, and others. Information was not solicited specifically for this draft but was compiled from previous recommendations. Not all of the specific recommendations made by any or all of these groups are included herein. This document establishes initiatives to achieve the above actions.

Estimates of the financial impact of an action, based on available data and professional judgment, are provided whenever possible. Readers should recognize that these estimates are fluid due to the nature of the data and the ever-changing program. In particular, since FCIC does not have a single aggregate mathematical or statistical model that describes its programs, estimates of financial impact are based on partial analysis which considers the effect of one particular action in the absence of any other action or initiative. Also, the exact steps to be taken under this Blueprint depend in part upon the public comment and recommendations received before investing resources in detailed studies of potential impacts. Readers are encouraged to provide information, rationale, and where possible, estimates of costs or potential savings.

In some cases the financial impact of an action may not be quantified. This does not mean the action is not important or that it cannot contribute to achievement of the goal. For example, enhanced management reporting systems do not produce a measurable financial impact. However, such systems can enhance FCIC's ability to estimate the potential impacts of program changes and assure that ongoing management decisions recognize the impact of the decision on future actions.

This document is divided into four main sections, which describe: (1) crop insurance program to provide context and background; (2) actions FCIC proposes as part of this plan to achieve the target loss ratio; (3) additional actions that FCIC may take if those described in section II are not effective or that cannot be implemented due to unforeseen circumstances; and (4) changes FCIC will consider once the projected loss ratio achieves the targeted level of 1.10.

I. BACKGROUND OF THE CROP INSURANCE PROGRAM

A. Overview of Program Operations

Crop insurance is delivered primarily by commercial insurance companies that have entered into a cooperative financial arrangement (the Standard Reinsurance Agreement [SRA]) with FCIC. Under this arrangement, the company agrees to deliver an FCIC designed and priced product to eligible buyers. The company is responsible for all aspects of customer service, and guarantees payment of the insured person's share of the premium to FCIC. In return, FCIC reimburses the company for administrative expenses and requires the company (on a State basis) to share in insurance experience whether favorable or unfavorable. FCIC also provides stop loss reinsurance that limits the maximum loss the company can sustain.

A small and decreasing portion of the total sales is managed directly by FCIC through sales and service contractors. These contractors agree to sell an FCIC designed and priced product and to perform certain servicing functions related to the sale (such as determining the average yields). FCIC reimburses the contractor for administrative expenses associated with selling and servicing the product; however, FCIC is directly responsible for premium collection, loss adjustment, and payment of losses. These latter functions are the responsibility of the reinsured company under that delivery system. FCIC intends to eliminate direct sales after the 1994 crop year because this system now delivers less than 10 percent of the total business, and maintaining a nationwide capability for delivery at an acceptable cost is difficult.

The crop insurance plan for most crops indemnifies insured persons for losses in yield exceeding a predetermined threshold amount. To establish this threshold an average yield is determined based on the individual's production history. The first portion of the loss (deductible of the insurance), equal to 25, 35, 50, or 65 percent of the average yield, must be sustained by the insured person. These are the choices of deductibles now offered by FCIC, and typically are described by the maximum loss in yield covered by the insurance; *e.g.*, 75 percent coverage, 65 percent, etc. The 50 and 75 percent coverage levels are required by the Act to be available to all persons. The level of coverage is chosen by the insured individual.

The insured person also must choose a price at which the yield is valued for the purposes of computing the amount of premium and any applicable amount of loss; this variable is called the price election. FCIC must offer a price election that is not less than the anticipated market price at time of harvest. This determination is made well before the possibility of loss is known during the crop year. Otherwise, insured persons would choose low price elections if no loss is sustained (minimizes premium payments) the highest possible price election if a loss occurs (maximizes indemnities).

FCIC establishes premium rates for the various coverage levels, yields, crop types and farming practices (*e.g.*, irrigated) for each county. All planted acres of the crop are covered by the insurance policy unless for some reason the acreage is uninsurable. The premium owed by the insured person is determined by multiplying the average yield per acre by the coverage level, multiplied by the number of acres planted, the price election, and the premium rate. For example, if the average yield is 100 bushels per acre, the coverage level is 65 percent, planted acres are 50, the price election is \$2.25, and the premium rate is 5.2 percent, the premium is equal to $100 \times 0.65 \times 50 \times \$2.25 \times 0.052$, or \$380.25. The potential indemnity in the event of a total loss is \$7,312.50 (determined by multiplying the average yield, coverage level, planted acres, and price election).

A portion of the total premium is subsidized to encourage participation in the program. The subsidy is 30 percent of the total premium for coverage levels up to and including the 65 percent level. The subsidy for 75 percent level of coverage is equal to the dollar amount that would be paid at the 65 percent level of coverage. The premium subsidy for the above example would be \$114.08; thus, the insured person would pay \$266.17. The same \$114.08 subsidy would be paid if the insured person chose the 75 percent coverage level.

In the event of a loss, the amount of production that was harvested, or that was determined that should have been harvested, is measured by the insurer. An indemnity payment is made if the determined production is less than the total guarantee for the acreage (yield multiplied by coverage

level and acres planted). For example, if the insured person harvests 1,000 bushels from 25 acres and does not harvest a potential yield of 10 bushels per acre from the remaining 25 acres, the total of the production to count is 1,250 bushels (1,000 bushels harvested plus 25 acres multiplied by 10 bushels). This is subtracted from the total bushel guarantee for the acreage ($100 \times 0.65 \times 50$, or 3,250 bushels), resulting in a loss of 2,000 bushels. The indemnity is equal to the number of lost bushels multiplied by the price election. For this example, the indemnity would be 2,000 bushels $\times$ \$2.25, or \$4,500.

Crop insurance does not guarantee revenue. As the above example illustrates, it provides an insurance indemnity only if production is less than the established guarantee. No protection is provided if the market price is less than the price election.

B. Legislative Background and Issues

Federal crop insurance was established as a pilot program in the 1930's. Prior to 1980, crop insurance was available only on major crops in major producing areas. The coverage level often was limited to 60 percent or less of a long-term average yield for an area. Congress amended the Act in 1980 to expand the scope and coverage of the program with the intent that it be the sole means of providing public disaster assistance to U.S. farmers. Participation in the program increased after the 1980 amendments, but remains below levels deemed necessary to be regarded as the principal vehicle for disaster assistance. Insured acreage peaked at about 40–45 percent of the total acreage planted to insurable crops in 1988–89, but more commonly has been in the 30–35 percent range. Losses also increased with the expansion of the program. The loss ratio has exceeded the break-even amount of 1.00 in every year since 1980. Cumulative losses for the years 1980–1992 were approximately \$2.9 billion, with a cumulative loss ratio of about 1.45 for the 13 years.

Program participation is an issue influencing the Federal Crop Insurance Program. Full participation (i.e., 100 percent of eligible acres insured) is the measure of program success that is accepted (at least implicitly) by some persons. This measure may not be the most appropriate. A rational decision to buy insurance of any kind must be based on the magnitude of the financial difficulties that accompany a loss. For example, buying collision coverage on a 15-year old automobile makes little financial sense. Similarly, buying insurance on a crop that contributes only a small portion of the expected income of the insured person may not make financial sense. Full participation in the crop insurance program may not represent an efficient use of the taxpayer's resources. However, participation must be high enough to minimize or eliminate perceived needs to legislate disaster assistance funded under dire emergency provisions of the Budget Enforcement Act. The level of participation in the crop insurance program that maximizes returns to the public is not known, and is an area needing further definition.

Many losses paid in the 1980's and early 1990's were due to widespread disasters, the adverse financial effects of which Congress intended to mitigate under the Act. However, continuing loss ratios exceeding 100 percent, enactment of disaster assistance in nearly every year since 1988, and lower than desirable participation indicate that the public policy goals of the program have not been fully realized. The Secretary of Agriculture has proposed a reform of the crop insurance program to:

- Achieve actuarial soundness.
- Increase participation to levels that render ad hoc disaster legislation unnecessary.
- Eliminate incentives to enact ad hoc disaster assistance legislation.

The proposals contained in this Blueprint focus on these three areas that directly relate to the goal of achieving the targeted loss ratio. They are: (1) actuarial matters such as premium rates and yield guarantees, (2) underwriting matters such as terms and conditions of insurance policies, and (3) management issues such as compliance and risk-sharing arrangements with commercial insurers.

II. MANAGEMENT ACTIONS TO ACHIEVE A LOSS RATIO OF 1.10

A. Develop More Accurate Insurance Yields

The insurance yield may be the single most important factor in determining the success or failure of the crop insurance program. A yield that is too high compared to the productive potential of the person or land will increase the number of years

that a loss is paid. An excessively high yield also increases the amount paid when a loss occurs. A yield that is too low will not effectively protect farmers from loss and, because it is regarded as very insufficient, will not induce desired levels of participation.

From the 1985 through 1993 crop years, insured yields were based on a program called the Actual Production History (APH) Plan. The goal of this program was to obtain 10 previous yields to establish the insured yield for the next crop year. Proxy yields largely based on ASCS farm program payment yields or county averages were allowed whenever farmers would not or could not provide 10 years of history. Analysis by FCIC and others determined the proxy yields were benefiting farmers whose yields tended to be lower than average and discouraging farmers whose yields tended to be above average. Consequently, a modified APH program that reduced the influence of the proxy yields was introduced beginning with the 1994 crop year; thus, a "ladder" was introduced into the proxy yields. Only 65 percent credit is given to the proxy yield if no actual yields are reported, 80 percent credit is given if one actual yield is reported, 90 percent if two actual yields are reported, and 100 percent if three actual yields are reported. The proxy yields are not used after four actual yields are available. The insured yield is a simple average of the 4 years of actual and modified proxy yields for the first 4 years, and then (after 4 years) is the simple average of the actual yields reported. Acquiring 10 years of production history remains the goal of the program. These revised procedures are the core of the initiatives to comply with the mandate of OBRA 93 to institute rules to demonstrate actual production histories.

The revised rules are expected to substantially reduce losses of the Federal Crop Insurance Program. Analysis performed by FCIC indicates the new rules would reduce losses by 15 percent for corn, 22 percent for soybeans, and 18 percent for wheat. These analyses were based on simulations of loss histories using the rules for the two computational methods—the previous APH and the proposed modified-APH plans. The analyses encompassed nine States each for corn and soybeans and three States for wheat. These State and crops represented nearly 60 percent of the total premiums earned in 1990. The results indicated that the modified-APH rules would reduce losses by a weighted average of 19 percent and are believed to be representative for most crops.

The actual loss ratio for the 1990 crop year was 1.23. If the modified APH rules did reduce losses by an average of 19 percent, the loss ratio would have been 0.996. This would achieve significant compliance with the loss ratio target of 1.10.

Based on these results, FCIC implemented modified-APH for the 1994 crop year by:

- Promulgating regulations for the program during calendar year 1994.
- Measuring the impact of the modifications upon net program losses by calculating insured yields, premiums, and indemnities of policyholders under 1993 and 1994 rules.
- Where possible, determining whether the modified APH rules had the intended effect of providing a more accurate offer for farmers who previously elected not to purchase crop insurance.
- Determining whether the average number of yields reported for prior years has changed under the modified APH rules compared with APH rules for 1990 through 1993.
- Implementing a tracking system to assure that insurance experience remains associated with a person in future years (See item D below).
- Developing reporting processes to assure that the accuracy of yield determinations is continuously monitored and improved.
- Actions requiring analysis of the effects of the modified APH rules upon the accuracy of insured yields cannot be completed until losses from the 1994 crop year are processed. For wheat and other fall planted crops, such availability will occur by about the fourth calendar quarter of 1994. For spring planted crops, this does not occur until about the middle of the first calendar quarter of 1995.

B. Catastrophic Yield Adjustment

FCIC recognizes that the average of a series of observations as short as 4 years is subject to significant variations due to abnormally large or small yields during that time. For example, if a major disaster year such as 1993 is included in the 4 years, the procedure implicitly states that a similar year will occur once every 4 years. This is not likely. Thus, FCIC will examine certain adjustments to the

modified-APH rules with a goal to assign more appropriate probabilities to the individual observations. These adjustments commonly are called catastrophic yield adjustments. However, just as the yields for 1 year may be abnormally low, they also may be abnormally high. Capping the abnormally high years may also be appropriate so that average yields are not excessively high due solely to a few observations.

FCIC will evaluate alternative methods to recognize catastrophic and unusually good crop years, and consider implementing appropriate adjustments to the modified-APH plan effective for the 1995 crop year.

FCIC believes that these actions to implement modified-APH will reduce the average loss ratio over time by 10–15 percentage points (e.g., from an average of 1.40 for several years to 1.25 to 1.30). This estimate is based on a conservative expectation of the actual results of the simulations described above.

C. Implement Group Risk Plan

FCIC is implementing a program of insurance that is based on the average yield of an area, not upon individual yield coverage as is offered under the traditional APH program. The area coverage is called the Group Risk Plan (GRP) by FCIC. GRP was introduced as a pilot program for the 1993 crop year for soybeans in 96 counties. It was expanded for the 1994 crop year to include seven additional crops encompassing 1,872 county crop programs (one crop in one county) in 27 States. Crops now included under GRP are barley (three States), corn (17 States), cotton (seven States), forage (two States), grain sorghum (four States), peanuts (four States), soybeans (24 States), and wheat (eight States).

The GRP is intended to protect the insured person against the financial consequences of a disaster that strikes all or nearly all farmers in an area. It sets an expected county yield for each year based on historical yields, adjusted for any trends, whenever the actual county average yield for the year is less than the expected county yield by a predetermined amount, an indemnity is paid. The principal differences of the GRP compared to traditional individual coverage are:

- Coverage is based on a trend projected yield, which probably will exceed the average yield of all farmers insured under individual yield coverage if there is a positive trend in yields for the area.
- Higher coverage levels (deductibles are as low as 10 percent) at affordable premium rates can be sold.

Thus, in the proper circumstances, GRP will offer risk protection that may be better than the individual coverage, and may do so at a lower cost.

GRP has characteristics that make it unsuitable for managing the adverse financial consequences of crop loss in certain circumstances. A farmer's yield each year must change in the same direction and by about the same amount as the county yield if it is to be fully effective coverage for the individual. For example, if the county's yield decreases by 25 percent from the expected yield for that year, the farmer's yield also should decline by about 25 percent from the yield he or she would have expected. In financial market terms, the "beta" of the farmer's yields and the county yields should be near 1.00.

Adequate data are a limitation to further significant expansion of GRP. The concept as presently developed uses many years (30 or more) of county yields. These data are routinely available only for counties in which the crop has been grown in commercially significant quantities. Weather data and crop growth models may permit expansion into counties in which the historical yield data are not available, but research is needed to develop and test these approaches. Further, acceptance of GRP by bankers as collateral for loans is yet to be determined.

Significant expansion of GRP is not anticipated until its contributions to agricultural risk management can be measured. No estimates of savings can be attributed to GRP because customer acceptance is not known. Customer acceptance of the soybean GRP for the 1993 crop year was limited. Fewer than 500 policies (of nearly 700,000 total for the crop insurance program) were sold. Even if the plan improves the actuarial soundness of crop insurance, the present volume of business is not sufficient to make any noticeable difference in program results.

D. Implement Data Base of Taxpayer Identification Numbers

Amendments to the Federal Crop Insurance Act enacted in 1990 authorize FCIC to collect and use social security numbers and employer identification numbers to administer its programs. These regulations were appropriately approved and were published in the FEDERAL REGISTER in late 1992. OBRA 93 further directed

FCIC to implement a database of these numbers for certain uses not later than the 1995 crop year.

FCIC implemented the database described above in January 1994, effective for the 1994 crop year. This database is used to locate production history that is not reported by a person, to assure that classifications assigned under the nonstandard classification system (NCS—See paragraph E) are used for both the individual who accumulated the adverse history and any person having a significant beneficial interest in a crop produced by that person, and for other related purposes. In particular, further efforts will be made to accumulate information about persons involved in sales and servicing of crop insurance—agents, loss adjusters, and other insurance providers—so that their contributions to achieving the target loss ratio can be measured.

Implementing this database will make both modified-APH and the NCS more effective by permitting FCIC and reinsured companies to assure that all appropriate experience and premium rating factors are used. Incremental improvement in the loss ratio due to modified-APH and NCS is difficult to quantify. The database will enhance those programs as well as permit FCIC to systematically measure the performance of insurance providers for the first time.

FCIC will also use the social security numbers and employer identification numbers for the implementation of an Ineligible File Tracking System. This system will be used to restrict (through an automated environment) producers who have been declared ineligible to obtain benefits provided by the Federal Crop Insurance Program. The FCIC expects to implement the Ineligible File Tracking System beginning with the 1995 fiscal year.

E. Expand the Nonstandard Classification System (NCS)

FCIC instituted the NCS for the 1990 crop year because evidence indicated that a small percentage of insured persons had losses in nearly every year. The losses paid to these persons far exceeded paid premiums. For various reasons, the insured yields for these individuals exceeded their apparent capabilities, and the premium rates were not representative of the risks posed by these persons. NCS was intended to reduce the insurance guarantee and increase the premium rate for such individuals. Modified-APH eliminates the need to reduce insured yields because the insured yield will be based solely on actual yields when a person is selected for NCS. However, NCS will continue to increase the premium rates as appropriate for those individuals who persistently have losses.

The Agriculture, Rural Development, Food and Drug, and Related Agencies Appropriation Act for the 1994 fiscal year prohibited FCIC from using any funds appropriated to insure crops in certain counties unless an NCS program had been implemented in those counties. Counties were affected if the loss ratio, after applying the 1993 premium rates, was greater than 1.10 more than 70 percent of the years that the crop had been insured in that county. Approximately 2,100 county crop programs were affected by this provision.

For the 1994 crop year, NCS has been extended to 11 crops encompassing over 90 percent of the total value of insurance in force. Additionally, all of the county crop programs affected by the Appropriations language have been included under the NCS. Over 25,000 individuals (about 3.6 percent of all active policies for the 1993 crop year) were included under this program. Not all of these persons had been insured during the base period. NCS also extends to persons who participated in growing the crop in some way but who may not have been insured. These persons also are classified under NCS so that the acreage cannot simply be insured under a different name to avoid the NCS classification.

In 1993, FCIC commissioned a study of the NCS to determine its effectiveness. A draft report of that study indicates that the NCS reduced the loss ratio by 5 to 10 points. This report is undergoing final preparation as this Blueprint for Financial Soundness is finalized.

FCIC will expand the NCS program for the 1995 crop year. All eligible crops will be included, although greater flexibility in selections may be authorized whenever program factors that led to poor experience have been identified. NCS is not suited to certain insured crops (*e.g.*, Texas citrus trees) that are subject to infrequent losses of great severity. The additional savings from NCS are likely to be small in terms of the total business because the crops that constitute the majority of premiums and losses already are included.

F. Institute Premium Rate Adjustments

Premium rates are essential to the success of the crop insurance program. Rates that are too low will not produce adequate income and will lead to persistent losses. High rates will, paradoxically, likely lead to the same outcome. Excessive premium rates discourage participation by a broadly based cross-section of the farming community. Instead, persons who are most likely to collect indemnities will buy, and it is not likely that rates can be increased as rapidly as the relative risk of the pool of insured persons increases.

FCIC has increased premium rates for all crops in a systematic fashion beginning with the 1991 crop year. Rates have increased as much as 70 percent for some crops in some counties from the 1991 to the 1994 crop years. Decreases of up to 20 percent have been made for some crops in counties with histories of low losses. By an amendment to the Act in 1990, Congress limited general premium rate increases to 20 percent annually.

The above statistics indicate the amounts that FCIC has increased the base premium rates. The average premium rate actually earned (actual premium paid divided by actual liability) may not have increased by the same magnitude for various reasons. Most importantly, insured persons may choose a lower coverage level when the rate increases. By doing so, they accept a lesser degree of protection but also pay a lower premium rate.

FCIC proposes to continue premium rate increases as needed to help achieve the required loss ratio. The rate increases made during 1991–1994 have done much to enhance the actuarial soundness of the program. However, the premium rates for some crops and areas of the country remain below the levels needed to achieve the overall 1.10 loss ratio target.

The impact of premium rate adjustments has been evaluated by using data for the 20 years from 1973–1992. The effectiveness of the adjustments was measured by applying the current 1993 premium rate levels to the historical period from 1973 and all subsequent years. The loss ratios were recalculated by using the revised premium amounts.

This method does not include any change in sales that may occur due to a higher or lower cost of insurance. It assumes the 20-year base period is adequate to measure actuarial performance, an assumption that may not be the most appropriate definition of actuarial soundness. Events such as a 1993 Midwestern flood may or may not be appropriate to include in the 20-year base period for a particular area of the country.

In 1993, seven crops (barley, corn, cotton, grain sorghum, oats, soybeans, and wheat) constituted 75 percent of total premiums. The loss ratio for 1980–1992 for these seven crops was 1.45, identical to the loss ratio for all insured crops for this same period. Thus, changes in premium rates for these crops should be representative of the changes that have been made for all crops in recent years. The premium rate changes for the seven crops through the 1994 crop year are estimated to have been adequate to reduce the 1980–1992 loss ratio from 1.45 to 1.08. This aggregate result meets the 1.10 standard required by OBRA 93, but only two of the seven crops individually meet this standard. Within each of these crops, many parts of the country will meet the standard but others will not. Hence, additional rate changes in 1995 and later years are appropriate.

FCIC recognizes that premium rate increases are an important component of a viable crop insurance program. It is also recognized that increasing premium rates to the levels suggested by the most recent 20 year experience may not be good public policy. Extremely high premium rates will preclude realization of the social benefits and public policy goals of the program because participation will be discouraged. If this happens, experience indicates that ad hoc disaster assistance will be enacted. Such assistance is less likely to satisfy social objectives with regard to maintaining rural communities and adequate supplies of food and fiber because it is uncertain for any particular year or region of the country. Thus, a catastrophic adjustment process may be needed to temper the influence of a year such as 1993. If the weather of 1993 truly is a one in 100 year event (or, as some have suggested, a one in 500 year event), its influence should be tempered in terms of the premium rates charged to insured persons.

In addition to changing premium rates as needed, FCIC proposes to take a number of additional actions to enhance the accuracy and adequacy of its actuarial activities. These include:

- Develop computer software and other tools to enhance the quality of the data used to establish premium rates and perform actuarial analyses ("STATPLAN" database, due for completion in October 1994)
- Plans to contract with a major actuarial consulting firm to review all aspects of FCIC's actuarial methods (targeted to be let in 1994).
- Enhance staff skills by additional training in analytical methods for existing personnel and more emphasis on recruitment of actuarial trainees (ongoing) for appropriate functional units.
- Continue to contract with external specialists such as the Economic Research Service, land grant universities, the Cooperative Extension Service, and others (ongoing).
- Develop models to measure sources of change in premium volumes and track the effects of premium rate changes as isolated from changes induced by factors such as price elections, coverage level choices, insured crops, and other factors that are not controllable by the rate-making function (development to begin immediately).

G. Improve Underwriting of Crop Insurance Contracts

Underwriting begins by establishing the basic terms and conditions of the coverage. These include defining conditions that result in a covered loss, measuring the amount of that loss, and defining the responsibilities of the insured and the insurer. Underwriting continues with proper classification of an insured risk. For example, planting crop B the year after crop A was grown on the same acreage may be riskier than if other crops were grown the previous year. Some land, such as flood plains, is more prone to losses. Quality of management also is important. A farmer who is organized, plans, performs preventive maintenance on equipment, and performs field operations in a timely manner may minimize losses.

A comprehensive underwriting system requires effective risk management strategies and goals, standards, and documentation. Initiatives to improve underwriting that began in the early 1990's will be continued as part of the strategy detailed in this Blueprint. The following specific actions will be pursued:

- Fully automate the actuarial documents to facilitate more comprehensive underwriting at the point of sale and to verify the classification of risk in an automated environment (completed by the 1996 crop year).
- Develop standards and classification systems to assess and classify individual risk, including completion of research intended to develop a "scoring model" for risk that is based on measurable attributes of a person or situation similar to a credit rating model (for implementation by crop year 1996 if this model is feasible).
- Continue to rewrite crop insurance policies to better describe the insurance coverage and limitations and to reduce vulnerabilities to actuarial soundness that exist due to imprecise, unclear, or omitted terms and conditions (ongoing, with major crops scheduled for the 1995 crop year).
- Encourage development of supplemental or alternative insurance coverages authorized by section 508(b) of the Act so that coverage may be improved with most of the risk remaining in the commercial sector.

Improved underwriting will improve program performance. However, meaningful measures to quantify possible benefits are not readily available. For this reason, FCIC cannot attribute a specific dollar amount to the benefits of improved actuarial systems and crop insurance policies.

H. Emphasize Program Compliance

The FCIC Compliance function is designed to confirm that the Federal Crop Insurance Program is operated and delivered as intended. Through internal reviews based on generally accepted auditing principles, it assures that program controls are in place against excess losses due to waste, fraud and abuse. Compliance emphasis will focus on:

1. **Program Delivery.** Beginning in 1987, the Compliance staff conducted reviews of program delivery to assess compliance with regulations, policy, and procedure. That year, according to GAO and OIG audits, errors in claims payment represented an estimated 15 percent of all losses paid equaling \$55 million of taxpayer dollars. Since that time, Compliance efforts have reduced these errors to approximately 5 percent of indemnities but still need continued improvement. Losses due to claim payment errors are not included in underwriting calculations of risk, so this

reduction in excess losses has a direct and immediate impact of lowering the program loss ratio without increasing program cost or premium rates.

To further reduce claims overpayment the Compliance Staff will review the entire operations of each delivery company in coordinated nationwide reviews. The review methodology was recently revised to reflect generally accepted auditing principles and statistically projectable sampling techniques.

Beginning with the 1995 crop year, Compliance requirements will be expanded to define specific quality control and performance measurement processes for each delivery company. Policy service error rates will be monitored. The performance of each company will then be compared to an established national standard.

2. Program Performance. Compliance reviews for several years have shown that a proportion of the excess losses are attributable to features in program construction that produce unintended results. The Compliance Staff will conduct program performance reviews that assess regulations, policies and procedures designed to prevent waste, fraud, and abuse and that the program, policies, and procedures perform as intended.

As an example, in 1989 GAO claims that construction of policy language in the California Safflower program alone resulted in approximately \$20 million in excess losses. It is not possible to determine how much of FCIC losses may be attributable to unintended features of program construction. However, recent program performance pilot reviews of the peanut program and regional irrigated practices resulted in an estimated 4 to 10 percent reduction in losses for those areas that may otherwise have gone undetected.

For the past several years Compliance has conducted ad hoc program reviews on topical issues. These reviews will be expanded to identify and target reviews for crop insurance programs with the greatest potential vulnerability.

3. Fraud Prevention. The risk of fraud is particularly acute in the insurance industry. Estimates for property-casualty insurance indicate insurance fraud may represent as much as 15 percent of all losses paid. Recent efforts at crop insurance fraud detection and subsequent prosecution have been increasingly successful. However, after-the-fact controls on program abuse are not fully effective. Compliance will work with the delivery companies to focus on practical, cost efficient fraud prevention. Compliance operations, program performance, and complaint reviews will emphasize identifying systemic vulnerabilities and assessing program safeguards. Discrepancies noted in review findings will be evaluated to determine the underlying causes.

Emphasis also will be placed on measures to control program abuse that include strict contract enforcement and pro-active policy analyses that identifies potential abuse and targets additional claims review. These measures will be coupled with the aggressive implementation of civil sanctions, agent/loss adjuster debarment, and designating producer ineligibility in findings related to program abuse.

I. Assure that Adequate Risk is Borne by the Commercial Insurance Industry

Amendments to the Act in 1990 directed FCIC to assure that adequate risk is borne by the commercial insurance companies reinsured by FCIC, consistent with their ability to bear risk and the availability of commercial reinsurance. For the 1992 reinsurance year (a 12-month period that began on July 1, 1991 and ended on June 30, 1992), FCIC substantially modified its Standard Reinsurance Agreement (SRA) with the commercial insurers which participate in the program. Both the amount and the probability of losses on the part of the commercial insurers were increased in this agreement. Additional incremental changes in the amount of potential gains and losses were made for both the 1993 and 1994 SRA's.

The GAO suggests in a report entitled *Crop Insurance Program has not Fostered Significant Risk Sharing by Insurance Companies* (GAO/RCED 92-25, January 13, 1992) that the changes in the 1992 SRA are not significant enough in the area of risk bearing by the commercial insurance companies. Still, the 1992 SRA fundamentally changed the manner in which gains and losses are calculated, a subtle but effective measure to increase risk. The amount of potential loss increased, but the change in the formula increased the chances that the company would lose in years of poor experience. As a comparison, the commercial industry lost approximately \$8 million in 1988 when the crop insurance program sustained a loss ratio of 2.45 primarily due to drought in the Midwest. If that experience is restated to the larger 1993 premium amounts, the loss still would have amounted to only about \$10-15 million. Results from the 1993 crop year are not yet complete, but current estimates indicate that commercial insurers will sustain losses of \$80-85 million although the loss ratio will be less than in 1988. The difference is caused by the SRA changes.

Some will argue that industry-wide losses of \$80–85 million are not significant compared to overall program losses that may be near \$900 million in 1993. Two factors bear on this issue: (1) The ability of the insurance companies to earn reserves under the SRA, and (2) The effect of losses upon an insurance company's operations in future years.

The commercial industry can bear a greater share of the losses only if there is corresponding opportunity to achieve comparable earnings in favorable years. Over the long term, the industry must achieve a satisfactory rate of return on invested capital, or it would make economic sense for participants to invest in other endeavors. The SRA must allow adequate opportunity to earn this satisfactory rate of return. It also must permit accumulation of reserves to pay losses in years that disasters strike. Under the present SRA and the conditions of actuarial soundness of the program, there is no opportunity to accumulate the reserves needed to bear a large portion of a \$900 million loss.

Losses directly impact the capital structure of the companies. An insurance company leverages its capital (the term "surplus" is used by the industry) to support the volume of business that it writes. As a general rule, an insurance company is permitted by regulators to bear the risk associated with \$2 to \$3 of premium per \$1 of surplus. The ratio of premiums to surplus may be lower for risky lines of insurance such as multiple peril crop insurance. Thus, whenever an insurance company loses a portion of its capital, its ability to accept premiums in future years is reduced by a greater amount, which in turn reduces its ability to earn profits and reserves. These factors must be considered when the ability of the industry to bear risk is evaluated, as is mandated by the Act.

As appropriate, given the factors discussed above, FCIC will evaluate (1) the need to increase risk sharing with the commercial insurance industry as the program achieves greater actuarial soundness, (2) reducing cessions to the assigned risk fund by requiring the industry to share in losses for loss ratios that exceed 5.00, (3) changing the stop loss provisions of the SRA, and (4) recruiting additional commercial insurers to participate in the crop insurance business. These changes will be made incrementally beginning with the 1995 SRA that takes effect on July 1, 1994.

J. Improve Loss Adjustment

Any actuarial and underwriting system can be affected by errors in adjustment of losses. These errors include both overpayment and underpayment of claims. Underpayment would not seem to be a factor influencing actuarial soundness, but failure to pay a loss when due will cause insured persons to question the value of the insurance and potentially reduce participation. The insurance experience also will not accurately depict the nature of the risk insured, leading to inaccuracies in future premium rates.

Some problems in loss adjustment are directly related to deficiencies in underwriting. For example, if the crop insurance policy is not clear on a particular point, the loss adjuster may find it necessary to make a determination in favor of the insured person. FCIC will undertake the following initiatives to assure high quality of loss adjustment determinations so that results are fair to insured persons and taxpayers:

- Develop uniform loss adjustment standards that clearly specify the requirements for accurate determinations.
- Continue research to improve loss adjustment methods, such as yield appraisal methods and techniques for unharvested crops, and measurement techniques for stored production.
- Strengthen the quality adjustment provisions of crop insurance contracts and develop standards to prevent abuse of production determinations when quality losses are claimed.

The contributions of these factors to achieve the 1.10 target loss ratio will be measured by a reduction in improper amounts paid on claims and a reduced error rate. The potential impact of these actions is difficult to quantify since the initiatives to improve underwriting also affect this area. These actions are ongoing. Loss adjustment standards for major crops and changes to the quality adjustment provisions are targeted for the 1995 crop year.

K. Marketing Crop Insurance

FCIC marketing efforts for 1994 will be directed by a strategic marketing plan based on information and data received from market research compiled across the country. The plan's main objectives will be to inform members of the farming community about changes in the program and to educate farmers about risk management, emphasizing the value of crop insurance to farming operations.

FCIC will conduct a year-long media campaign targeted at publications and broadcast markets with an agricultural audience.

Also, emphasis on outreach to minority farmers, traditionally under-represented in the program, will be coordinated through a Minority Outreach Marketing Plan that specifically identifies minority farmers in each of the 10 FCIC Regional Service Offices.

L. Expand Participation by Introducing New Products

Numerous ideas for products that will enhance the quality and acceptance of the crop insurance program have been suggested. These include cost of production coverage (several different concepts), dollar denominated coverage, revenue insurance, replacement cost insurance, and others. FCIC currently has contracts with the Economic Research Service to evaluate several alternatives in the context of public policy contributions, availability of data to support the concepts, assessments of producer acceptance, and other factors. FCIC proposes to continue such research and seeks comments about additional concepts that may be appropriate. Implementation of a pilot test of the best alternatives will be pursued.

M. Improve Accuracy of Other Program Variables

This section includes items that impact the program but are not easily categorized under a previous heading. These are:

- **Unit division.** A unit is a tract of land used to establish the amount of insurance and any indemnity. For example, the crop insurance policy defines a unit as all land in a county that is owned by the farmer or rented for cash and planted to the insured crop. This unit may be subdivided under certain conditions, including payment of additional premium. Generally, insured persons favor a program that gives them greater flexibility and freedom for establishing a unit. Some research indicates that size of a unit may affect losses, i.e., a unit consisting of 10 acres may have a greater loss (in relative terms) than a unit consisting of 100 acres. This research, if verified, suggests that a surcharge may be needed for small acreage units regardless of how these are formed (by dividing larger units or because this is all the land planted to the crop). FCIC will examine the research and determine if this surcharge is appropriate, both actuarially and as a public policy initiative. FCIC also will explore the potential to provide greater flexibility of unit determinations as a tool to enhance program acceptance by customers. The pricing needed to support greater flexibility must be determined before it can be implemented. Implementation of changes will be targeted for the 1996 crop year.

- **Program dates.** Program dates include sales closing, acreage reporting, cancellation, and others. Several of these dates may directly affect the actuarial soundness of the program. For example, neither the farmer nor the insurer should be able to predict the potential for loss on the sales closing date. However, a study by one university indicates that farmers may achieve better than a 50-50 probability of predicting a loss with the current sales closing date of April 15 in the Midwest. Arguments in favor of having a sales closing date as late as possible generally focus on the need to maximize sales opportunities; i.e., that interest in purchasing crop insurance is greatest as planting time approaches. In a draft report, the GAO has encouraged FCIC to close sales earlier. FCIC proposes to close sales for the 1995 crop year by 15-30 days earlier than the present dates. FCIC requests comments regarding other actions with regard to program dates that will facilitate achievement of the targeted 1.10 loss ratio.

- **Staged guarantees.** Staged guarantees reduce the amount of insurance when a crop is lost before harvest. For example, a farmer who abandons a crop within 30 days of planting might be paid only 40 percent of the amount of insurance. The concept underlying staged guarantees is investment costs; the farmer's investment is less than the total needed to produce and harvest the crop. Some believe this approach will reduce outlays for indemnities and help achieve actuarial soundness. However, in the long run its effect could be to reduce premium rates from levels otherwise needed. The impact of staged guarantees upon customer acceptance of crop insurance may be the valid measure of this concept. FCIC specifically requests comments on this feature and assessments of its potential contribution to achieving the targeted 1.10 loss ratio.

- **De minimus yields.** This term denotes a yield below which any production is disregarded for the purpose of determining the amount of indemnity. The concept is advanced by interested parties as an equity issue—that it costs the farmer more to harvest the crop than it is worth in the market. If allowed by the program, indemnities will increase compared to the present provisions of the crop policies,

which, in turn, requires higher premium rates to achieve the goal. Readers are encouraged to comment on the desirability of increasing premium rates by an amount needed to permit this feature to be included in crop insurance policies.

- **Suspension and debarment.** Inappropriate determinations and poor administration of the crop insurance program is alleged about agents, loss adjusters, and others who are involved with delivery of crop insurance. The SSN/EIN database is intended to help FCIC monitor the conduct of these persons. However, monitoring in and of itself is insufficient if there are no penalties for violations of program rules. FCIC proposes to develop clear and concise suspension and debarment procedures for agents, loss adjusters, reinsured companies and others who fail to observe the highest standards of performance in program delivery and administration.

- **Price Elections.** The GAO recommended in a 1991 report that for the major crops, FCIC set its price elections equal to the forecasts issued by the World Agricultural Outlook Board in its semi-annual estimates. These estimates correspond to the cycle used to prepare the annual budget of the U.S. Government. These estimates are available only twice each year. Based on a sampling of a few years, GAO stated that overall losses would be reduced if this recommendation were adopted. FCIC is committed to offering a price election that complies fully with the requirements of the law. In addition, the offer must be meaningful to farmers. FCIC requests comments regarding this recommendation and assessments by readers of its likelihood of contributing to reduced loss ratios and improved participation.

Readers are requested to identify additional issues that they believe are relevant and important to assist FCIC in its actions to manage the program to achieve the target loss ratio while maintaining or increasing participation levels.

II. MANAGEMENT ACTIONS IF SECTION II ARE NOT SUCCESSFUL

The actions identified in section II of this document represent a major reinforcing of FCIC efforts to achieve the important goal of financial and actuarial soundness in Federal crop insurance.

FCIC believes that successful completion of these actions will meet the objective of achieving actuarial soundness as required by OBRA 93. Several years must elapse before it will be possible to observe FCIC's achievement of the objective. In the interim, attainment must be measured by realistic models of risk that adequately represent the crop insurance program. Flexibility in managing the program to attain the objective while simultaneously achieving other important policy objectives must be stressed.

Few options that do not adversely affect participation in a material manner are available in the event the actions described in this blueprint are determined to be inadequate. One option is to focus better on defining the risk that is included in the premium rates charged to current insureds. Extreme crop disasters (such as the 1993 flooding and cold, wet growing season) tend to be widespread and occur infrequently. Crop insurance is not actuarially sound in a commercial sense because the private sector cannot manage the magnitude of these risks or arrange the financing over the long periods of time needed to accumulate reserves for a major disaster. This characteristic of crop disasters argues that actuarial soundness perhaps should be measured on a basis that separates normally expected conditions from the extreme disasters. This would serve to more precisely define the risk included in the premium rates for current insureds, and the risk that should be amortized over longer time periods.

If the above is not acceptable, another action would be to limit the liability of crop insurance to specific areas and crops. This limitation could take the form of complete withdrawal of insurance in some cases, or limitations on the volume of business that would be accepted in a year for a crop or area. Commercial insurers use this process to manage their exposure to avoid concentrations geographically or by product line.. Crop insurance may need the same management of its exposures rather than accepting any and all risk whenever farmers decide to enter and exit the program. This extreme action would indicate that the program was unable to completely fulfill its social and public policy responsibilities, and must be regarded as an initiative of last resort.

III. MANAGEMENT ACTIONS IF ACTIONS IN SECTION II ARE MORE SUCCESSFUL THAN NEEDED

The greatest impediment to increased program participation will be high premium rates that might result from the actions defined in this plan. Moderation of premium rate increases will be a priority if more stringent program administration reduces the loss ratio below the target. If this occurs, experience should be examined to identify losses paid that no longer should be expected. Once the impact of those losses is eliminated from the experience, some improvement in premium rates would be anticipated. FCIC believes that the remaining management actions that have improved administration of the program or that have better defined the coverage provided to United States agriculture should not be relaxed because these generally represent good administration of public policy.

REFORMING FEDERAL CROP INSURANCE/DISASTER ASSISTANCE

BACKGROUND ON USDA PROPOSALS IMPROVING DELIVERY AND LIMITING ABUSE

Last month, Agriculture Secretary Mike Espy put forward a massive reform program to overhaul Federal crop insurance and disaster aid for the benefit of both farmers and taxpayers. Many elements of that program and of other changes at the Federal Crop Insurance Corporation (FCIC), directly address concerns raised by the Office of Inspector General (OIG) in its recent reports, as detailed below. We look forward to the opportunity to present the Secretary's reform program in detail to the Senate Committee on Agriculture, Nutrition, and Forestry in the near future and we appreciate the extremely constructive role that this Committee and the OIG have played in this effort.

1. Limit Scope of Disaster Programs Generally:

Under the pending "Federal Crop Insurance Reform Act of 1994", insurable crops will be covered by insurance *only*, not by disaster aid. A legal barrier is created against future ad hoc disaster programs for these crops. Insurable crops (see attached list) represent some 75 percent of the value of this country's agriculture production and over 90 percent of payments under recent disaster programs.

Coverage for insurable crops will be available for a nominal fee. Participation will increase, driving down the need for disaster assistance for insured crops.

2. Within Disaster Program, Tighten Controls Against Fraud

The Reform bill creates a new standing disaster program for uninsured crops. Since this program is permanent, rather than ad hoc, FCIC will be able to institute basic year-to-year management controls, as such making compliance, yield, acreage and price data more reliable and enforceable. Other features designed to limit abuse include:

Acreage report requirement: Planted acreage must be reported by a preset acreage reporting date. FCIC will increase inspections to verify actual acres and farming practices. After-the-fact claims of increased planting are not allowed.

Use of Actual Production History: Yields will be based on at least 4 years of the producer's actual production history (APH). Producers who fail or refuse to provide records receive a diminished yield guarantee. New producers will receive yields based on county averages. This system helps farmers with good track records, penalizes those with no records, and thereby encourages each to document their production history.

Area Trigger: The disaster declaration for an affected region will be tied to local conditions. This will improve compliance by making it harder for a single producer to abuse the program. In true disasters, farmers will be protected.

Farm management encouraged: Assistance can be denied for neglect or failure to follow good farming practices.

Reduced assistance based on inputs: We will consider supporting an amendment to the legislation to authorize the FCIC or the Secretary to adjust market prices used to calculate payments where needed to prevent abuse.

3. Intensify Compliance Efforts:

FCIC's compliance program is designed to monitor, detect, and deter program abuses and system weaknesses. It consists of over 50 staff in six field offices across the country. This branch of FCIC is responsible for reducing the crop insurance

“error rate” (overpayments in claims based on intentional or unintentional mistakes) from about 16 percent in the late 1980s to about 5 percent according to the most recent OIG report.

We will increase our compliance emphasis by: (1) applying our new computerized tracking system based on a producer's Social Security number to document annual, individual yields; (2) developing joint compliance strategies and operations with other agencies of the USDA including the Agricultural Stabilization and Conservation Service, the Office of Inspector General and private firms; (3) setting new training and testing standards for crop insurance agents and loss adjusters; (4) maintaining meaningful risk-sharing with private insurers; and (5) taking full advantage of our authority to suspend, debar, or sanction parties who abuse our program.

4. Reorganize USDA to Combat Fraud:

Under Secretary Espy's proposed USDA reorganization, insurance and disaster programs will be consolidated under a single “Risk Management” arm of the Farm Service Agency. This will strengthen management and prevent the exploitation of the current divided system.

The merger of ASCS and FCIC into a single agency allows USDA to pool compliance resources.

For further information, contact Paula Thomasson (202) 254-8399.

FEDERAL CROP INSURANCE REFORM ACT OF 1994

SUMMARY OF KEY ELEMENTS

1. *Repeal of ad hoc disaster authority:* Current legal authorities for ad hoc crop loss disaster relief are repealed. In the future, the program outlined below will replace these disaster bills as the Federal response to emergencies involving widespread crop loss.

As added protection, a parliamentary hurdle is erected: future ad hoc relief measures are placed on budget. The current Budget Act exemption for these bills is scaled back.

2. *Catastrophic crop insurance coverage:* The Federal crop insurance program is supplemented with a new catastrophic coverage level available to farmers for a nominal processing fee of \$50 per crop per county, up to \$100 per farmer county. This catastrophic plan will protect against yield losses greater than 50 percent at a payment rate of 60 percent of the expected market price—a level comparable to disaster relief programs in recent years. The processing fee may be waived for limited resource farmers.

Farmers may purchase additional insurance coverage providing higher yield or price protection levels for additional cost. Targeted subsidies are provided to encourage farmers to pursue these higher coverage levels.

3. *Linkage to farm programs:* To ensure wide participation, crop insurance coverage at the catastrophic level or above is linked to participation in Federal commodity support programs or Farmers Home Administration loans. This step should result in crop insurance participation rising from 33 percent to about 80 percent of insurable acres.

4. *Delivery:* Farmers may choose to obtain the catastrophic coverage either through a private reinsured company or through a USDA county office. Higher insurance coverages remain available only through private insurers.

5. *Industry competition:* Premium rates are restructured to reflect both direct premium subsidies and the insurers expense reimbursement allowance, a more realistic calculation. More-efficient companies will be allowed to pass along lowered overhead costs in reduced rates charged to farmers, creating a more competitive market environment.

6. *Uninsurable crops:* A standing disaster program would exist for crops not covered by crop insurance triggered, with payments triggered by area-wide loss levels and protection levels similar to those under the catastrophic insurance plan.

7. *Fiscal soundness:* The new catastrophic coverage will be governed by actual “APH” yields and all other program changes outlined in the “Blueprint for Financial Soundness.”

8. *Cost:* The new program will cost about \$8.1 billion for fiscal years 1995 through 1999. This represents a 5-year *savings* of some \$750 million compared to the projected cost of the current Federal crop insurance program plus the average annual cost for ad hoc crop loss disaster relief programs over the past decade.

UNITED STATES CROP VALUE SUMMARY

INSURED CROPS

NATIONAL VALUE OF ALL CROPS \$92,385,311,215

CROP	REPORTED ACRES	DOLLAR VALUE	PERCENT OF TOTAL VALUE
Corn, Grain	66,950,480	18,008,691,703	19.493
Soybeans	56,498,545	11,213,520,994	12.138
Wheat	69,353,948	7,296,722,323	7.898
Cotton, Upland	11,501,930	4,884,989,171	5.288
Tobacco	732,740	2,829,953,119	3.063
Potatoes	1,363,816	2,396,315,957	2.594
Nursery, Container		2,375,462,434	2.571
Corn, Silage	6,124,202	1,954,333,349	2.115
Oranges	770,214	1,515,565,984	1.640
Apples	352,114	1,408,875,579	1.525
Peanuts	1,807,325	1,256,883,370	1.360
Sorghum, Grain	9,086,031	1,203,379,180	1.303
Sugar Beets	1,375,468	1,125,379,300	1.218
Rice	2,812,429	1,040,085,810	1.126
Tomatoes - Fresh	137,578	924,639,769	1.001
Barley	7,505,000	906,414,000	0.981
Grapes - Processed	408,090	885,062,003	0.958
Sugarcane	723,840	813,706,190	0.881
Raisins	266,737	677,942,810	0.734
Beans, Dry	2,099,403	660,075,798	0.714
Almonds	413,202	639,048,900	0.692
Tomatoes - Processed	353,911	617,956,960	0.669
Grapes, Table	90,343	494,035,398	0.535
Onions	146,180	493,421,041	0.534
Peaches	117,823	482,137,001	0.522
Oats	6,015,517	412,485,275	0.446
Grapefruit	168,928	354,979,543	0.384
Lemons	59,816	347,117,610	0.376
Pears	50,031	281,428,961	0.305
Plums - Fresh	45,199	265,029,699	0.287
Sweet Corn - Fresh	191,672	256,059,591	0.277
Walnuts, English	184,837	254,412,036	0.275
Sunflowers	1,854,495	247,439,110	0.268
Peppers	53,513	225,972,741	0.245

UNITED STATES CROP VALUE SUMMARY

INSURED CROPS

NATIONAL VALUE OF ALL CROPS \$92,385,311,215

CROP	REPORTED ACRES	DOLLAR VALUE	PERCENT OF TOTAL VALUE
Sweet Corn - Processed	476,613	213,509,890	0.231
Nectarines	25,761	158,609,100	0.172
Cranberries	27,801	152,828,500	0.165
Beans, Snap - Processed	214,640	139,856,244	0.151
Prunes	79,707	133,203,850	0.144
Peas, Green	293,750	109,804,780	0.119
Tangerines	18,922	69,225,312	0.075
Apricots	20,249	48,509,599	0.053
Peas, Dry	274,500	43,363,600	0.047
Macadamia Nuts	18,700	41,720,000	0.045
Safflower	159,073	37,924,863	0.041
Flax	253,002	20,858,600	0.023
Tangelos	10,419	16,897,699	0.018
Figs	13,071	16,351,600	0.018
Beans, Lima - Processed	21,650	9,432,000	0.010
Templets	9,199	7,641,999	0.008
TOTAL		69,969,260,345	75.736

"Nursery, Container" crops are container grown landscape plants.

Values are not available for the following insured crops: Popcorn, Hybrid Seed Corn, Hybrid Seed Sorghum.

Acreage data is incomplete for apples, peaches, pears and plums.

CROP EXPANSION FEASIBILITY STUDY LIST

Feasibility studies are currently underway on the following crops in anticipation of developing new crop programs:

AVOCADOS	LETTUCE-HEAD
ASPARAGUS	LETTUCE-LEAF
BLUEBERRIES	MUSHROOMS
BROCCOLI	NURSERY CROPS
CANOLA	PECANS
CANTALOUPE	PEPPERMINT
CARROTS	PINEAPPLE
CAULIFLOWER	PISTACHIOS
CELERY	SEED-FORAGE
CHERRIES-SWEET	SEED-LAWN
HAY-ALL	STRAWBERRIES
HAY-HAYLAGE	SWEET POTATOES
HAY-OTHER	WATERMELON

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